Itsla Yunisva Aviva, Yuana Tri Utomo, Muhamad Yusup,
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AZ-ZAHRA MEDIA SOCIETY

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PREFACE

Hamdan wa syukran Lillah, sholatan wa salaman ‘ala Rasulillah.

With gratitude to Allah Swt., we are pleased to present the book entitled Contemporary Issues & Developments in Islamic Economics to readers. This book is crafted to enrich the knowledge and understanding of academics, practitioners, and enthusiasts of Islamic economics by addressing contemporary issues in this rapidly developing field. Covering foundational concepts to present-day challenges and opportunities, this book is a collective effort to offer readers comprehensive insights into the evolving landscape of Islamic economics.

The book begins by providing an essential introduction to Islamic economics, exploring its core principles, objectives, and philosophical foundations. This chapter serves as a vital basis for understanding the unique values that shape an inclusive and just economic system within Islam. The discussion then extends to the historical development and evolution of Islamic economic thought, tracing its journey from classical interpretations to modern adaptations. This section helps readers appreciate how

Islamic economic principles have transformed over time, adapting to different societal needs and technological advancements. A subsequent chapter delves into the fundamentals of Islamic finance, emphasizing the principles that guide Shariah-compliant financial practices. It introduces essential concepts like the prohibition of riba and ethical investment, aiming to provide a robust framework for understanding the distinct aspects of Islamic financial systems.

This is followed by a discussion of Islamic banking practices, highlighting the application of Shariah principles within banking and demonstrating how Islamic banks operate in contrast to conventional banking. Readers gain insight into how Islamic banks uphold ethical standards while promoting economic inclusivity. The book also addresses the dynamics of the Islamic capital market, introducing various instruments aligned with Shariah principles to offer halal investment avenues. This section explains how such markets promote justice, fairness, and transparency in investment while supporting sustainable economic growth. Beyond mainstream finance, this book explores Islamic microfinance, emphasizing its role in empowering small-scale economies and fostering economic independence. This section highlights microfinance as a critical tool for reducing economic disparity through the principles of justice and shared prosperity.

The concluding chapter examines the opportunities and challenges faced by Islamic economics in the modern era, analyzing how it adapts to the influences of globalization, digitalization, and societal change. This chapter offers valuable insights into the future trajectory of Islamic economics, encouraging adaptive and innovative approaches to further its relevance in a globalized economy.

We hope this book serves as a valuable resource for deepening the knowledge of Islamic economics among students, professionals, and policymakers alike. Our deepest appreciation goes to everyone who contributed their insights to this publication, as well as to those involved in its realization.

May this book bring great benefits, inspire new perspectives, and foster the continued advancement of Islamic economic knowledge to meet the needs of future societies.

Deli Serdang, October 30th 2024
26 Rabiul Akhir 1446 H

H. Angga Syahputra, S.E.I., M.E.I., CBPA
Director of Az-Zahra Media Society Publisher

EDITOR'S PREFACE

Alhamdulillah 'ala kulli haal,

In the name of Allah, the Most Gracious, the Most Merciful. With great appreciation, we present this book, *Contemporary Issues & Developments in Islamic Economics*, which has been carefully compiled to address the expanding interest and critical need for scholarly exploration in Islamic economics today. As Islamic economics moves forward on the global stage, this work aims to guide readers through the foundational concepts and contemporary developments shaping this field.

The book opens with a clear introduction to the fundamentals of Islamic economics, establishing a foundational understanding of its principles and goals. This section provides readers with a valuable context to appreciate the distinct framework that Islamic economics presents as a comprehensive system of thought.

Following this, readers are introduced to the historical context and the evolution of Islamic economic thought. By exploring this progression, the book aims to show how Islamic economics has maintained its core values while adapting to societal shifts, offering a dynamic perspective on economic justice and ethics.

A central focus of this work is on the principles of Islamic finance, including essential concepts like riba-free transactions and ethical investments, which are examined in detail. These insights serve as a foundation for understanding how Islamic finance institutions function and contribute to a more equitable economic system. Islamic banking, another significant component of this book, demonstrates how Islamic banks operate under the principles of justice and ethical conduct, setting them apart from conventional banks. This section serves to educate readers on the unique features and benefits of Islamic banking as a viable alternative.

The exploration extends into the Islamic capital market, discussing the development of Shariah-compliant investment instruments. By examining these financial tools, this chapter highlights the role of Islamic capital markets in promoting transparency and fairness in economic growth. Another noteworthy section focuses on Islamic microfinance, a vital area in the field that emphasizes supporting marginalized communities. This segment shows the impact of microfinance in reducing economic disparity and fostering financial empowerment for small-scale entrepreneurs.

The book closes by addressing the contemporary challenges and opportunities facing Islamic economics in a fast-evolving world. Here, the emphasis is placed on how Islamic economics can respond to modern issues, including digitalization and globalization, with innovative strategies that align with its foundational ethics and values. It is our hope that this book serves not only as an academic reference but as a source of inspiration for those engaged in shaping the future of Islamic economics. We extend our sincerest gratitude to the contributors, whose knowledge and expertise are reflected in each chapter, as well as to all who supported this publication.

May this work illuminate new pathways in Islamic economic thought and practice, and contribute positively to the development of a just and sustainable economic future.

Ghina Ulfah Saefurrohman, Lc., M.E.Sy.
Editor

DAFTAR ISI

INTRODUCTION TO ISLAMIC ECONOMICS

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A. Introduction

Islamic economics can be regarded as a relatively new branch of knowledge when compared to conventional economics. Generally, the global economy is divided into two main categories: socialist economics and capitalist economics. These two schools of thought have different theories and paradigms, both of which are internationally recognized. Meanwhile, the existence of Islamic economics is acknowledged by some, but there are still many who remain skeptical.

In an era of globalization and rapid social change, the world faces various complex economic challenges. In this context, the study of Islamic economics becomes increasingly important. Islamic economics not only offers an alternative to the conventional economic system but also provides solutions to various issues faced by society today. This article will discuss the fundamentals of Islamic economics as a field of knowledge and as a system for addressing contemporary problems and developments.

The study of Islamic economics is becoming more significant in the ongoing context of globalization. Many countries are showing a growing interest in ethical and sustainable financial systems. By learning the fundamental principles of Islamic economics, we can identify how concepts such as social justice, the prohibition of riba (usury), and social responsibility can offer meaningful solutions to the economic problems faced worldwide today.

B. Defining Islamic Economics

Linguistically, the term economics comes from the Greek words "oikos" and "nomos." The word "oikos" means household, while "nomos" means to manage or regulate. Thus, broadly speaking, economics refers to the rules or management of a household. Therefore, the discipline that studies how individuals manage their resources to meet their needs is called economics.

In Islam, the economy is referred to as *"iqtishad,"* which comes from the word *"qosdun,"* meaning balance (equilibrium) and justice (equality balanced). The Quran mentions the term *"al-qashdu"* in several verses, including the following (Fauzia & Riyadi, 2014):

1. In Surah Luqman: 19, *"Waqṣid fī masy-yika,"* which can be simply interpreted as moderation.
2. In Surah Al-Maidah: 66, *"minhum ummatum muqta sidatun,"* meaning those who are in the middle or moderate.

3. In Surah An-Nahl: 9, *"wa ‘alallâhi qashdus-sabîli,"* which is understood as the straight path.
4. In Surah At-Taubah: 92, *"wasafaran qashidan,"* referring to a journey that is near and easy, without difficulties.

Islamic economics is built on the foundation of Islam, as economics is an integral part of the religion. As a derivative of Islam, Islamic economics will follow its teachings in various aspects. Unlike conventional economics, which emphasizes analysis of economic problems and alternative solutions, Islamic economics studies individual behavior guided by Islamic principles. This includes determining life goals, perspectives, analyzing economic issues, and addressing these problems. Islamic economics encompasses the conscious economic behavior of individuals striving to achieve *mashlahah* or *falah*, often referred to as homoislamicus (Pusat Pengkajian dan Pengembangan Ekonomi Islam (P3EI) UII & Bank Indonesia, 2012).

Islamic economics is a framework that integrates economic principles with the ethical and moral foundations of Islam. Unlike conventional economic systems, which often prioritize profit maximization, Islamic economics emphasizes justice, equity, and social welfare (Ali, 2015; Syahputra et al., 2024). It seeks to establish a balance between individual aspirations and societal needs, fostering an environment where economic activities contribute to the well-being of all. In addition, Islamic economics is also a branch of knowledge that studies human behavior related to various desires and the limitations of resources, as well as their alternative uses. Its aim is to achieve falah, which refers to well-being in both this life and the hereafter. It is clear that in Islamic economics, the main objective is not solely to achieve material profit or economic growth, but also to create social justice, community welfare, and economic sustainability (Hasan, 2016).

The following are definitions of Islamic economics according to various experts:

1. M. Abdul Manan, Islamic economics is a social science that studies the economic issues of society inspired by Islamic values (Manan, 1991).
2. M. Nejatullah Al-Siddiqi states that Islamic economics is the Muslim thinkers' response to the economic challenges of a particular era. In this arduous effort, they are aided by the Quran and Sunnah, reason *(ijtihad)*, and experience (Siddiqi, 1988).
3. M. Umer Chapra defines Islamic economics as a field of knowledge that assists in the realization of human happiness through the allocation and distribution of limited resources within the framework of Islamic teachings, without restricting individual freedom to create a sustainable macroeconomic and ecological balance (Chapra, 2001).
4. Adiwarman Karim argues that Islamic economics is an economic activity based on universal values, not solely an economic activity derived from the Quran and Hadith. Therefore, he has a different perspective that Islamic economics encompasses elements such as *tawhid* (oneness), *khilafah* (governance), *'adl* (justice), *nubuwah* (prophethood), and *ma'ad* (return) (Karim, 2019).

C. History Context and Development of Islamic Economics

In the capitalist economic system, "Free Competition System" is implemented which prioritizes free competition, where those who can utilize capital effectively will excel in business. Meanwhile, other economic systems have experienced collapse, except Islamic economics, which prioritizes the interests of individuals and society. The presence of Islamic economics has given rise to a new hope for many people, especially Muslims, for an alternative economy to the economic system of capitalism and socialism as the mainstream that contains a world economic system, especially since World War II which gave rise to many Islamic countries that were former imperialist colonies. In this case, the existence of Islamic economics as an alternative economic model makes it possible for many parties, Muslims and non-Muslims, to recall various Islamic teachings. Especially those that include the relationship between human needs through economic activities and other activities (Bakar, 2020).

Thoughts on Islamic economics are not a new phenomenon. The roots of Islamic economics can be traced back to the early Islamic civilization, where trade and commerce flourished under principles outlined in the Qur'an and Hadith. Long before the establishment of formal conventional economics, various Muslim scholars addressed the economic and social issues of their era, offering policy recommendations to rulers and guidance to the general populace. Prominent scholars like Ibn Khaldun (1332–1406 AD) and Al-Ghazali (1058-1111 AD) contributed significantly to the understanding of economic concepts, such as the role of the state in economic regulation and the importance of ethical conduct in trade (Khan, 1984). Ibn Khaldun also formulated a theory of social change and history which was majorly based on rise and fall of dynasty. He showed how the dynamic forces of history nations, dynasties, ideas, cities and markets, operate in ways that counter basic assumptions about warfare and investment. He showed how social and economic factors intermingled to explain the rhythms of growth and decline that he saw in nations, dynasties, cities, societies and business enterprises (Ali, 2015).

Over the past two decades, the field of Islamic economics has effectively attracted researchers from diverse areas such as finance, marketing, monetary studies, and entrepreneurship to conduct further investigations (Ghlamallah et al., 2021; Mubarrok et al., 2022) There has been a notable rise in Islamic economic publications, as evidenced by significant increases in both the Scopus database (Haque et al., 2020) and the Web of Science (Yenice et al., 2022). Over the centuries, the principles of Islamic economics have evolved, adapting to contemporary challenges while remaining anchored in the original teachings of Islam.

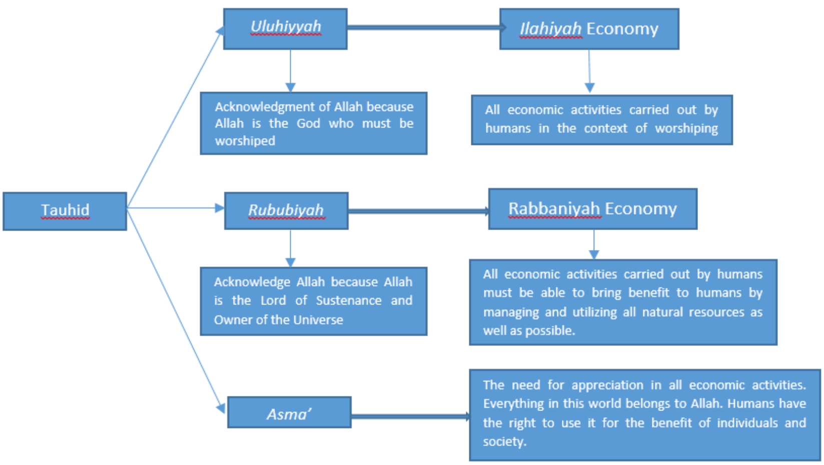
D. Principles of Islamic Economics

Tawhid is one of the three basic principles in Islam, including in the economic scope. In the *tawhid* view, humans as economic actors are just trustees. Therefore, humans must follow the provisions of Allah Swt. in all economic activities. Allah's provisions that must be obeyed in this case are not only mechanistic in nature and social life but also theological (uluhiyah) and moral (khuluqiyah). In the aspect of *tawhid*, the understanding of Islamic economics includes two things, namely ilahiyah and rabbaniyah economics (Fauzia & Riyadi, 2014).

Tawhid linguistically originates from the Arabic language, derived from the verb *"wahhada-yuwahhidu-tauhidan*," which means to unify. In terms of terminology, *tawhid* is understood as the concept of the oneness of Allah Swt. in *uluhiyyah* (oneness in worship) and *rububiyah* (oneness in creation and governance). In the economic context, *tawhid* teaches that all resources come from Allah, and humans are responsible for managing these resources wisely and justly (Syahputra et al., 2024) . In other references, the principle of divinity (in this case, *tawhid*) positions the interests of individuals and society in a very close relationship, emphasizing principles of harmony, balance, and not competition, thus creating the fairest economy (Bakar, 2020) For greater clarity, the following is a schematic image related to the basics of Islamic economics:

Picture 1:

The Basis of Islamic Economic



E. The Goals of Islamic Economics

The goal of Islamic economics is *maslahah* for people. According to Jalal al-Din Abd al-Rahman, in linguistic terms *maslahah* is defined as everything that contains benefits for humans. Meanwhile, in terms of terms, *maslahah* is anything that is beneficial to humans that can be achieved by humans by obtaining it or by avoiding it. As well as avoiding slavery which is too dangerous for humans. (Al-Rahman, 1983). It can be understood that *mashlahah* is all forms of circumstances, both material and non-material, that are capable of increasing human position as the most noble beings. The basic *mashlahah* for human life includes five things, namely religion *(deen),* soul *(nafs),* intellect *('aql),* heredity *(nasb),* and wealth *(maal)* (Pusat Pengkajian dan Pengembangan Ekonomi Islam (P3EI) UII & Bank Indonesia, 2012).

There are two ways to maintain *mashlahah*, namely *"min haytsu al-wujud"* and *"min haytsu al-adam".* The first way is to strive for all forms of economic activity so that it can bring benefits. For example, when someone enters the industrial sector, he must always prepare several strategies so that his business is successful in gaining profits and benefits so that it will bring goodness to many parties. Furthermore, the second way is to fight everything that can hinder the progress of evil itself. For example, when someone enters the industrial sector, he must consider several things that could cause the business to go bankrupt (Fauzia & Riyadi, 2014).

Islamic economics does not only focus on financial aspects, but also on moral, social and environmental aspects, creating a holistic framework for the welfare of the people. If summarized from several references, the objectives of Islamic economics include several main points, namely as follows:

1. Blessings and Prosperity
   Islamic economics aims to achieve blessings in economic activities, namely creating sustainable prosperity for individuals and society. Every transaction and economic activity is expected to provide greater benefits for all parties (Ningrum et al., 2021; Suardi, 2021; Sudjana & Rizkison, 2020).

2. Social Justice
   This economic system seeks to reduce social inequality and ensure a fair distribution of wealth. The principle of justice requires that all members of society have equal

access to economic resources and opportunities (Arfah & Arif, 2022; Hemas, 2016; Husni, 2020).

3. Moral Responsibility
   Islamic economics prioritizes ethical and moral values in every economic activity. Economic actors are expected to act with integrity and be responsible for the impact of their actions on society and the environment (Barom, 2018; Kalkavan et al., 2021).

4. Development of Individual Potential
   This system provides space for individuals to develop their potential and talents, while still prioritizing the welfare of society. This creates a balance between personal interests and social interests (Mahyudi, 2016; Shinkafi & Ali, 2018).

5. Prevention of Exploitative Practices
   Islamic economics aims to prevent detrimental practices, such as riba (interest), *gharar* (uncertainty), and other exploitative practices. This ensures that transactions are carried out fairly and transparently (Barom, 2018; Mirakhor et al., 2020).

6. Sustainable Development
   Islamic economics also prioritizes sustainable development that respects natural resources and maintains ecosystem balance. This is in line with the principle of maintaining trust and responsibility towards the earth (Arfah & Arif, 2022; Sudjana & Rizkison, 2020; Zauro et al., 2024).

F. Conclusion

Islamic economics is a relatively new branch of knowledge that offers an alternative to conventional economic systems, namely capitalist and socialist models. In the context of ongoing globalization, the study of Islamic economics is becoming increasingly important as it provides solutions to contemporary economic challenges through principles grounded in social justice, morality, and responsibility.

The foundational principle of Islamic economics is *tawhid*, which emphasizes the balance between individual and societal interests. The primary goal of Islamic economics is to achieve *maslahah*, which refers to the welfare that can be attained by individuals in both material and non-material aspects. This encompasses blessings and prosperity, social justice, moral responsibility, individual potential development, prevention of exploitative practices such as riba (usury) and *gharar* (uncertainty), and suistanable economy.

Thus, Islamic economics does not solely focus on financial aspects; it also integrates ethical, social, and environmental values. This creates a holistic framework aimed at enhancing overall societal welfare while addressing economic challenges in the modern era with a more sustainable and just approach.

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HISTORICAL DEVELOPMENT AND EVOLUTION OF ISLAMIC ECONOMIC THOUGHT

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A. Introduction

The study of Islamic economics is increasingly growing and in demand by various circles, both by practitioners who are curious about their business practices, as well as by academics who are anxious about contemporary economic problems that always raise problems (Aravik et al., 2022). This contemporary economic problem is like a vicious circle that never finds a solution. Research and tracing of existing sources regarding Islamic economics found information that the concept of Islamic economics and its practices have existed since the era of the Prophet Muhammad Saw. In the Makkah period, the economic activities of the Prophet PBUH and his companions were like that of humans in general, namely meeting the needs of life, going to the market to trade, and so on. The Arab economic condition at that time was advanced, as evidenced by the existence of the Kaaba as a center of international trade, the existence of traditional markets such as the Ukadz market, the Dzumatil Jandal market, and so on. In the Medina period, after the hijrah, the Prophet Muhammad Saw. made phenomenal policies, namely: fraternizing Muhajirin's friends with Anshor, establishing a mosque as the center of government, and building its own economy as the center of regulating the country's economy (Karim, 2021). This condition has been continued by the companions and their followers until now in Muslim countries in the world. The case in Indonesia of the Islamic economic system inherited by the Prophet Saw. can be seen in traditional markets that are close to the sultanates, for example: the *Kagungan Ndalem Beringharjo Market* in the Islamic Mataram Sultanate of Yogyakarta, the traditional market of the *Gerbang Raja Mangkurawang* in Kuati Kartanegara, and even Samudera Pasai is an international trade center because of its very strategic position in the Malacca Strait. These activities show that Indonesia inherited the well-organized trade from the Prophet Saw., and is still running today.

The Islamic economic system with trade as the main activity is the country's economic resource that guarantees the growth and equitable distribution of wealth to all people (Utomo, 2022). This Islamic economic practice was damaged by the Netherlands colonialism which carried out policy interventions, such as *cultuurstelsel* (forced planting), the case of *"nuthuk"* (setting prices too high), due to the influence of Capitalism that could not be stopped. The current contemporary economic condition is then hegemonized by the Capitalism system from the West. This article explains the evolution of Islamic economic thought, and the procedure for reviving it as it was during the time of the Prophet Muhammad Saw. and his companions.

B. The Overview History of Islamic Economics

The economy in the world is polarized into two systems, namely: capitalism and socialism. If there is a third economic system, it is called a mixed system because there is no single country that consistently practices capitalism or socialism (Nienhaus, 2010). Indonesia practices a mixed system, between capitalism and socialism, depending on the policies of the ruling regime. In the Soekarno era (1945-1967) there was a tendency towards socialism, in the Suharto era (1967-1998) there was a tendency towards capitalism, and after reform (in 1998) there was a shift in the development paradigm with the emergence of Islamic economic discourse. In fact, Islamic economics existed in Indonesia since Islam entered the archipelago (Nusantara) around the 13th to 16th centuries AD brought by traders through trade routes from Malabar, Arabia, Gujarat, and so on to ports on the north coast of the archipelago.

These traders simultaneously preached and blended with the community, even fighting against the colonization of the VOC (*Verenigde Oost-Indische Compagnie*) of the Netherlands with monopoly Capitalism through violence and war until the era of independence in 1945 AD. The direction of Islamic economic studies in Indonesia tends to be normative with a sharia and fiqh law approach. In fact, the history of Islamic economics from his home country has been very long since the era of the Prophet Muhammad Saw. preaching in Makkah and then migrating to Medina to apply the Islamic economic system as an implementation of the Qur'an, and al-Hadith (Prayitno et al., 2022).

1. Economics Condition of The Arabian Peninsula Before Islam

Hitti (2002) in *History of The Arabs* explained that the Arabian Peninsula is a strategic area for international trade. The peninsula has a vast, oil-bearing desert, Lake Tiberias in Palestine, and the Tigris River in Iraq. The Hijaz, which is now Saudi Arabia, is the birthplace of Islam, namely Mecca and Medina. The tradition of trade in the Arabian Peninsula has been rooted for a long time. This tradition is supported by the existence of the Kaaba as a center of worship since the Prophet Ibrahim As. has been passed down from generation to generation. The custom of the Quraish tribe to travel in caravans to trade abroad brings commodities from exchange in the form of animal skins, camel saddles, clothes, incense, dates, and so on.

The Arabian Peninsula became the center of world trade routes. The southern gateway through Yemen leads to the Indian Ocean to India, the archipelago, China, and Africa. The northern gate through Sham leads to Rome, Spain, and others mainland Europe. Trade in the markets of Makkah before Islam came was still filled with various frauds due to the *jahiliyyah* tradition. Economic tyranny due to multiplied usury transactions has become local customs. This tradition of economic fraud is explained by the words of Allah SWT in the Qur'an surah *al-Muthaffifin*. Trade fraud occurs in almost all forms of existing transactions, it can be ascertained that one of the parties from the seller or buyer suffers a loss. These forms of transactions are for example with the technique of throwing sticks or stones at the desired commodity, *mulamasah* transactions if the commodity has been touched must be purchased, and so on.

2. Economic Behavior of the Prophet Saw

The search for the economic behavior of the Prophet Saw. while in Makkah did not find a single manuscript that shows it, except for the behavior of da'wah calling the ummah to Islam. The activities of herding goats and trading with the uncle to Syria found in various sirah literature are the economic behavior of the Prophet Saw. before becoming a messenger of Allah Swt. As for the economic behavior of the first people who converted to Islam, such as: Khadijah, Abu Bakr, Uthman bin Affan, Abdurrahman bin Auf, Zubair bin Awwam, Sa'ad bin Abi Waqash, Talhah bin Ubaidillah, and so on, it is explained that they were from among the merchants. Their professions and businesses include clothing merchants, property entrepreneurs, iron craft industries, basic food traders, oil and food entrepreneurs, and so on. Then there was also evidence of the boycott of the Da'wah of the Prophet Saw. with the disconnection of the life network including the economic blockade of the Companions, there was no buying and selling of all commodities between the Quraish and the Prophet SAW and his companions (Abdulkader Cassim Mahomedy, 2013).

The event of migration (*hijrah*) from Makkah to Medina became a milestone in the application of Islamic law in all aspects of life, namely: politics, social in the case of interaction between men and women, law, education, economy, and so on. The Islamic economics that was theoretically discontinued by the Prophet Saw. when preaching in Makkah was then applied after the hijrah in Medina along with the descent of the Qur'an. Medina is not a trading area like Makkah, but an agricultural area that produces dates, grapes, wheat and several areas in the form of plantations and livestock. After the hijrah, the

Prophet PBUH made three spectacular policies, namely: fraternizing the muhajirin with anshor, building a mosque, and building his own market for Muslims that is different from the Jewish market (Al-Muafir, 1994). Imam Tabrani narrated from Abu Usayd: A man came to the Prophet Saw and said:

> "May my father and mother be your ransom! I see a place for the market, don't you want to go to it?" When the Prophet Saw. saw him, he liked it, and said, "Your market is blessed, so don't be blocked and don't let there be any taxes on it."

The *hijrah* event from Makkah to Medina is a new milestone in Islamic da'wah in implementing all laws and sharia in a kaffah manner, including in the economic field that shifts the economic power of the Jews. The economic system of the Prophet Saw. spread and was preached by the trade caravan group, affecting the economies in the Arabian Peninsula. This continuous Islamic syiar has a positive effect on the condition of the economic development of the people of Medina. The economic stability of the people of Medina under the leadership of the Prophet Muhammad Saw. is getting better when the state of Medina has income independently from *ghanimah, kharaaj,* and so on. This ideal condition became a role model that was continued by the *Khulafaur Rashidin*, Umayyad, Abbasiyyah, and Ottoman until it remains in contemporary times.

3. Islamic Economics: Systems or Sciences

The study of the economic behavior of the Prophet Saw. is a study of the Islamic economic system. This study is the result of the process of understanding the original sources of Islamic teachings, namely texts that have authority as sources of Islamic teachings, in the form of the Qur'an, al-Hadith, *ijma' sahabat*, and *qiyas syar'iy*. Islamic economics as a system inherited by the Prophet Saw. brought norms and implementing organs. The economic norms of the Prophet Saw. are important lessons from the hadith of the economic system, namely: (1) as the center of the community's economy is the benchmark for the success of state development, (2) it does not recognize the social class measured by the ownership of property and its equitable distribution to all souls, (3) there is no tax but zakat on business in accordance with the provisions of the terms and principles, (4) the market for traders is like a mosque for worship, such as roads for traveling, such as school buildings for education, (5) the Islamic economic system developed along with the trade caravans that preached spreading the teachings of Islam to all corners of the earth, (6) economic practices were not carried out for a full day and night until 24 hours, because the condition of the Islamic society system placed economic life limited to meeting daily needs so that it was strong to worship Allah Swt. The norms of the Islamic economic system guarantee the realization of the welfare of the population.

The implementing organs of the Islamic economic system inherited by the Prophet Muhammad Saw. are: *baitul mal, hisbah* or *muhtasib, caravan,* and *qirad*. *Baitul mal* is an institution that directly handles the welfare of the community, managing zakat, *ghanimah*, *fai', kharaaj, jizyah, 'ushr*, and *khums*. *Hisbah* or *muhtasib* is an institution responsible for keeping the rights of pilgrims safe with a pattern of supervision or patrol in public places, on highways, including in markets and so on. Supervision of *hisbah* in the market by monitoring prices to keep them stable, supervising traders so that they do not cheat by burdening the scales, prohibiting traders from intercepting on the road, and even supervising supply and demand at the same time, or supply itself and demand itself. *The caravan* is the implementer of an economic mechanism with trade that is free from elements that violate sharia, the guardian of distribution networks and Islamic trade pacts/blocks. *Qirad* or *shirkah* is a capital system in Islam using *dinar* and *dirham* currencies.

The study of the Islamic economic system is now left in history so that it becomes just a science. Economics is born from an economic system. Islamic economics is now biased because the economic system that overshadows it is no longer the Islamic system, but the capitalist system. This study is very important to convey so that Islamic economic practices in society become clean from elements of Capitalism as said by Umar bin Khattab (2006) who strictly prohibits people who are active in the economic sector if they do not know the laws. Umar said:

> "It is not permissible to sell in our markets except for people who truly understand religion *(faqiih fii ad-diin)*."

C. Islamic Economics in The Contemporary Era

Islam has a distinctive view of the economy that is different from the views of capitalism and socialism. The views of capitalism and socialism were born from the results of human intelligence, while the Islamic views were born apart from human intelligence as well as information from the Qur'an and al-Hadith as Islamic teachings. The verses of the Qur'an that discuss economics are often associated with human behavior in general related to their interactions when meeting the needs of daily life by buying and selling. For example, the words of Allah Swt. QS. An-Nisa verse 29 which means:

> "O you who believe, do not eat the treasures that are among you by a foolish mechanism, except by trade that is mutually pleasing among you and do not kill your souls, indeed Allah Almighty is Merciful towards you".

The study of economics in Islam should be a study of the economic system as practiced by the Prophet Saw. with his companions, not just as a science. The study and practice of Islamic economics in the contemporary era is now distorted to be narrow to the financial sector only. The financial aspect is an *entry point* of study like capitalism which focuses on *capital accumulations*. Money is considered the single most strategic capital. This makes the money economy and the capital economy the content of Islamic economic studies without paying attention to other aspects of the system. The roots of this kind of thinking do not realize that they have made capitalism the womb that gave birth to the Islamic economy. Economic studies in Islam should be clean from the influence of Capitalism and Socialism. Islamic economics as a science should be born from the economic system inherited by the Prophet Saw.

1. Sharia Economics in the Conventional System

The practice of the Islamic economic system from the time of the Prophet PBUH until now is integrated with political policies in the framework of Islamic teachings. Economics and politics cannot be separated from Islam, its journey is along with the journey of Islam from the first history in Makkah, then hijrah to Medina, the era of Khulafaur Rashidin, the Umayyad Bani, the Abbasiyah, the Ottoman and until now in the study in this book. The tradition of economic behavior that is overshadowed by this economic system has always been passed down from generation to generation and continues to be maintained by the spirit of Islamic economic philosophy in micro-level communities, traders in traditional markets. However, the emergence of capitalism brought by the Netherlands colonizers resulted in the Islamic economy being biased and obscured by modernity, the advancement of internet technology gave rise to platforms that helped shift the paradigm of Islamic economics. In fact, Islamic political economy is different from the political economy of capitalism. The political economy of capitalism develops by following the logic of the free market, from the classical era, socialism, neoclassical, keynessian, post-Keynessian era and the current era of free economic liberalism. The Islamic political economy is not affected by the logic of the free market. The economy in Islam is supervised by economic supervisory officers or *hisbah.*

Islamic political economy is a political economy based on Islam, the history of political economy has had ups and downs along with the application of the Islamic economic system in life in every era. Islamic political economy because it is based on Islam, there is an element of dogma in terms of beliefs and the presence of Islamic methodology with the Qur'an and as-Sunnah as a source of reference and inspiration in its epistemology. The logic of the free market of capitalism cannot be applied to Islamic political economy with the sharia market as the spearhead. Islamic political economy is different from Islamic political economy. Islam is one and there is no difference, but when it is called political economy it has the consequence of meaning that the policy of the ruler is applied to regulate the economy of its citizens, and when it is called political economy, it is still limited to theories about the economy and Islamic social theories have not become political decisions. Islamic political economy as a new idea of the discipline of Islamic economics that is looking for its form in various existing universities. The discussion not only displays the history of the thinking of various Muslim economists, economic interaction in society, but also discusses the Islamic economic system with a distinctive methodology. Islamic political economy is another word for sharia economics in the midst of the implementation of the conventional economic system. Deliarnov (2014) explained that Indonesia's condition when entering the era of globalization was in a condition of blindness and not knowing its position to fall into losses. Deliarnov recommended that Indonesia reform the economic-political-legal system that not only requires economic and political transformation, but also requires a transformation of moral values, especially in the legal aspect. The process of transforming Islamic political economy into Islamic economic politics requires the collective awareness of the community to return to the straight path that has been guided by Allah Swt. This process must certainly be intellectually monitored by Muslim economists who are concerned about this condition so as not to shift away from its noble goal.

2. Islamic Economics Methodology

An in-depth study of contemporary Islamic economics cannot be separated from its methodological process. After the collapse of Ottoman Turkey in 1924 AD, the study of Islamic economics as a contemporary science developed. The study of Islamic economics is still partial using a partial method with the epistemology of positivism.

Islamic economics should be born from postulates whose sources are from the Qur'an and As-Sunnah. Postulate is interpreted as the correct postulate and the truth has become data. The methodology for studying the Islamic economic system is ijtihad, namely: exerting all the ability to find assumptions of sharia law to the maximum. Ijtihad is not an epistemology of science like modern science. The epistemology of Islamic economics today, if traced to its origins, is found to have the influence of foreign philosophy as a result of the industrial revolution which uses scientific methods that are claimed to be neutral and objective equipped with statistics, mathematics, and econometrics as symbols of qualitative object quantification.

The ijtihad method with ushul fiqh (*mutakallimin and fuqoha'*) was first concocted by Imam Shafi'i (150-204 AH) and then perfected by scholars afterwards. They emphasized the sources of Islamic law, namely: *the Qur'an, al-Hadith, ijma'* and *Qiyas*. The Hanafiyah, Malikiyah, Hanabilah, Dzahiri, and Shia are different from Shafi'i because they use *ihtisan, urf, al-mashalih mursalah, shar'u man qablana, ijma' ahlul madinah*, and so on. The development of ushul fiqh into two schools of madrasas, namely *mutakallimin* and *fuqoha'*. These two madrassas when concluding the process of excavating sharia law argued and did not find a way out until the discovery of the maqashid theory (the purpose of Sharia) which was limited to illat as the pillars of qiyas. The development of the famous maqasid in the era of Imam Syatibi (d. 790) with his theories, namely *hifdzud diin, nafz, aql, nasl,* and *hifdzul maal.* Imam Shatibi's theory became a standard because it succeeded in bridging the debate between *mutakallimin* and *fuqoha* schools and even became a formal law applied by the Islamic State.

The next development is a distortion of *the concept of maqashid* because there is *a hifdzul maal narrative* that is commonly used by Mainstream Madzhabs. The marriage of conventional economies with Islamic dogma fails unless it dwells on finance, *zakat, infaq, shodaqoh,* riba and its institutions at the micro and slightly macro levels, not touching the global level of the capitalist agenda with free market liberalization. Those who adhere to the classical method in studying Islamic economics experience confusion and are always *mauquf* when faced with contemporary economic cases. Ijtihad as an Islamic economic methodology is faced with contemporary problems. Contemporary methods with a scientific foundation produce a partial contemporary economic madzhab on the economy and its non-systemic character. The classical method (*mutakallimin* and *fuqoha'*) stutters when facing contemporary problems, so that it becomes a compromise, liberal, or always *mauquf* in a systemic study.

The two methods above are not compatible in facing the challenges of the conventional economic system. Therefore, the study of Islamic economic methodology, without abandoning the methodology of classical scholars and contemporary scientific methods, requires *the istiqroi method* with the scientific terms of *historical development* and *re-engineering of Islamic economics* as the author's novelty. This istiqroi method exists because Islamic economics was born from the womb of Islamic teachings that are kaffah. Islamic economics can be born normally if the method of giving birth is also right. The Islamic economic system should not be born from the womb of capitalism, or socialism, nor even from the marriage of the two. The Islamic economic system has uniqueness, both in terms of its conceptions and in terms of its methodology.

The method that can be used to give birth to the Islamic economic system is not through the Islamization of conventional science, but with the method that was exemplified by the Prophet PBUH with his companions when preaching in Makkah and Medina which is then continued until the present contemporary times. The Islamic economic system explored by the ijtihad method from the Qur'an and as-Sunnah can give birth to Islamic economics after going through a theorization process, namely the discussion of Islamic economic doctrine using conventional economic language. If the theorization process, which is a postheory rather than a priori, is rearranged in a systematic arrangement, then a complete or systemic building of Islamic economics can be realized. The process of applying this theorization is similar to the process of ijtihad but not ijtihad, nor is it *istinbath* but the process of *tathbiqul hukmi alal masaai al-mustajiddah* (the application of law based on general nash on contemporary problems or new problems). For example, regarding the law of multi-level marketing, bitcoin, and so on.

3. Islamic Economics and Contemporary Madzhabs

In summary, these contemporary Islamic economic madhhabs use scientific methods except for the Hamfara madhhab which not only uses scientific methods but also uses rational methods with istiqroiy ushul fiqh. Actually, there is also a contemporary Islamic economic madhhab that is anti-mainstream, namely Murobithun which uses ushul fiqh ahlul Medina. A brief explanation of the contemporary Islamic economic madhhab is as follows: (1) mainstream madzhab. Mainstream madhhab figures include Umer Chapra (b. 1933 AD), Muh. Anas Zarqa, Muhammad Abdullah Mannan (b. 1938), Monzer Kahf (l.

1940), Nejatullah Shiddiqi (b. 1931) and so on. The thoughts of this madzhab are the background and are often used as references by Sharia Banking in Indonesia, Malaysia, Bangladesh, India, Pakistan, Turkey, and so on. The majority of universities and colleges also teach Islamic economics of this madhhab; (2) Critical alternative madzhabs. The figures of this madhhab are Timur Kuran (b. 1954 AD), Jomo, and Muhammad Arif. This critical alternative madhhab as the name implies, is very critical of existing economic ideas, let alone the economics of capitalism and socialism, Islamic economics alone if it is not in accordance with the original sources of Islam (al-Qur'an and Hadith) must be criticized as well; (3) madzhab Baqir Shodr. This madhhab is also called the Iqtishaduna madhhab because Baqir as-Shodr (1935-1980 AD) wrote a book entitled *"Iqtishoduna."* This madhhab argues that economics cannot be in line with Islam, because both come from basic philosophies that contradict each other; (4) the Hamfara madhhab with an Islamic economic methodology that is different from the previous three madzhabs. The methodology is born from a paradigm of science that is born from the system that oversees it. Ijtihad as a methodology in Islamic economics is not just an epistemological step that produces contemporary economic madhhabs as explained above, but can also provide a solution to the failure of Capitalism.

D. Historical Development

Historical development is a study of economic history that looks at the dynamic process from the initial condition to the transformation process to the finished condition. Syahrur (2010) described this with the terms *kainunah*, *sairurah,* and *shoirurah*. Historical development is intended to find out the past condition of the Islamic economy, the current condition where the Islamic economy is under the economic umbrella of Capitalism, and to design the future of the implementation of the Islamic economic system again. The answer to the question of whether this contemporary Islamic economy is in accordance with the real Islamic sharia or not, can be concluded with the dimension of the process, that in the authentic condition (still original or still pure) before the intervention of Capitalism, the answer is emphatically "yes," although the next condition has become corrupted and is now transforming back to the initial condition with a soft economic movement is not realized except by researchers who are sensitive to this condition (Zarqa, 2003).

1. Micro, Macro, and Global

A reading of contemporary economic practices reveals that these practices are a reflection of the economic understanding of the actors. This reading leads to a problem mapping of the economic knowledge of economic actors. Mapping understanding into three classes of knowledge represented by global, macro, and micro scopes. The knowledge of western economic actors is relatively more globalized because it comes into contact with the direct hegemony of capitalism and is diametrically different from Islamic economic actors who try to maintain tradition defensively. The position of the conflict of interest is at the macro level by policymakers. The scope of economics as a discipline is very broad across national territorial boundaries, which of course each nation has its own traditions and cultures. The influence of globalization and the free economy is able to force the opening of the domestic economy of other countries. The position of economics (especially if it is a system at once) in this global scope overshadows the knowledge under it, namely in law, socio-cultural science, political science, and so on. The production sciences such as innovation, agriculture, technology science as a means of production, health sciences, and the like are in a very micro technical area.

Islamic economics has practically existed since the era of the Prophet Saw. until now, and has even always existed and been maintained from generation to generation. The dynamics of Islamic economic practices that have ups and downs do not eliminate their existence in the micro realm, such as: buying and selling carried out in people's economies, small *shirkahs* carried out by farmers, and so on. In the micro scope, Islamic economic practices remain and are maintained along with the activities of Muslims carrying out their lives, both in the sense of meeting daily needs and in the sense of worshiping Allah Swt. The dynamics of Islamic economic practice occur in the macro region due to the tug-of-war between the interests of institutional authorities, between those who support and those who do not support, academic debates, such as the use of the term Islamic economics or sharia economics, and so on. As for the global scope, the dynamics of Islamic economic practices have not been realized but have been carried away by the wind of issues, such as the blue economy and green economy.

2. Re-Engineering Islamic Economic

Islamic studies have relevance anytime and anywhere without being limited by time and space. Islamic studies have always been dynamic and undergoing shifts. Islamic teachings, which according to some people are sacred and holy dogma, occupy the position of *taqdis*, actually make this teaching a hard, static object and not infrequently make its adherents become jumud. Although according to some other circles, it is not a dogma or if it is a dogma, the truth can still be questioned. Islamic studies, including the study of Islamic economics, penetrate all existing branches of science.

The discovery of contemporary Islamic economic madhhabs appeared along with the development of the social conditions of Islamic society after the collapse of the Ottomans in the transition era from the 19th century AD to the 20th century AD. At that time, the world economic pendulum was in the neoclassical era with the famous figure being Max Weber with his book *"Ethics of Capitalism and the Protestant Spirit."* Efforts to revive the glory of Islam through the economic field are engineered in such a way as to develop a paradigm from the revelation of authentic sources of Islamic teachings. Islamic economic engineering in the scientific aspect was carried out at a time when the world economic system applied global capitalism. This Islamic economic engineering departs with a scientific methodology that can be accounted for academically and accountability in faith is returned to Allah Swt., namely with Islamic economic da'wah that is intreparable, holistic, and comprehensive with a revolutionary nature.

3. Political Economy: Study and Da'wah

The economic politics that are applied today in the Islamic world are still partial. The economic policies issued by the authorities of these existing Muslim countries have not reflected the teachings of Islamic economics as the economic system taught by the Prophet PBUH which was then continued by the Companions and the next generation, namely the Umayyad, Abbasiyyah, and Ottomans. The study of Islamic economics needs to penetrate into political economy so that it is not only theoretical and academic but also leads to a movement to clean all existing elements from the influence of capitalism, both in fiscal policy and in monetary. Islamic political economy, which in practice is still partial, has shifted comprehensively due to the encouragement of the study of Islamic political economy by its actors in all fields with their respective roles. The shift in political and economic practice from partialism of ideas to whole, integral, comprehensive, kaffah ideas as explained above is a movement of thought. This thought movement is a re-engineering of the thought movement that preceded the engineering, from partial engineering to complete engineering. This is what is meant by *re-engineering Islamic economic*, which is to make the discipline of Islamic political economy; from practice to science, from political economy to political economy with the perspective of Islamic studies.

E. Epilogue

The evolution of Islamic economic thought is a historical inevitability. The Islamic economic system that was once implemented in the era of the Prophet Muhammad Saw. with his companions in the country of Medina has become a role model of the current generation with a complete view as well as the view of humans from above hellycopter. This complete view is able to see the dynamics of Islamic economic history from each existing periodization: the authentic era when revelation was still descending, the era of glory when the Umayyads, the Abbasids, and the Ottoman Turkey dominated world civilization, and the contemporary era now when the inevitability of the spirit of returning to glory appeared. Historical development and re-engineering of Islamic economics is the main agenda to realize the role model of the Islamic economic system inherited by the Prophet Saw. to be practiced again in this contemporary society. The source of the Islamic economic system that is a role model is revelation, so that it can be methodologically accounted for in this world and in the hereafter. The closing sentence of this article is a call to fight together to return to the Islamic economic system that is clean from the biases of capitalism. Islamic economics as a teaching that is rahmatan lil'alamin can be a solution to the problem of damage to the capitalist economic system which always invites repeated crises**.** Welcome to Islamic economics rahmatan lil alamin.

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FUNDAMENTALS OF ISLAMIC FINANCE

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A. Introduction

Islamic finance is a financial system that operates in accordance with the principles of Sharia or Islamic law. This system is not only financial in nature but also has strong moral and ethical dimensions (Iqbal, Z., & Mirakhor, A., 2020). In Islamic finance, every transaction must reflect values of justice, transparency, and social responsibility. Unlike conventional financial systems, Islamic finance prohibits practices considered harmful or unjust, such as *riba* (interest), *gharar* (uncertainty), and *maysir* (gambling) (Ayub, M., 2019). The prohibition of these elements aims to create a more stable, just, and balanced financial system.

The prohibition of *riba*, or interest, is one of the main foundations of Islamic finance. From a Sharia perspective, *riba* is viewed as the exploitation of the borrower, as the lender gains profit without any effort or risk. Instead, Islamic finance uses partnership-based models such as *mudharabah* (a partnership between an investor and a business manager) and *musharakah* (a partnership where both parties share capital and profit) (El-Gamal, M. A., 2021). These models emphasize a balance of risk and reward for all parties involved and avoid the exploitation of one party by another.

In addition, *gharar*, or uncertainty in transactions, is also prohibited in Islamic finance. *Gharar* refers to any transaction that is unclear or uncertain, whether in terms of the object, price, or time of delivery. This principle is applied to ensure that all transactions are conducted transparently and fairly, so that no party is disadvantaged by incomplete information or ambiguity in the agreement. The prohibition of *gharar* protects investors and consumers from unforeseen risks and excessive speculation that could harm the economy as a whole (El-Gamal, M. A., 2021).

The principle of *maysir*, or gambling, is another important prohibition in Islamic finance. *Maysir* refers to any form of excessive speculation or gambling, where the outcome depends heavily on luck rather than rational calculation or productive effort. Islamic finance seeks to promote investment and economic activities that are based on real productivity and generate genuine economic value, rather than mere speculation or chance (Hassan, M. K., & Lewis, M. K., 2022). Therefore, practices such as short selling and speculative derivatives are not permitted within the Islamic financial system.

Globally, Islamic finance has grown rapidly as a more ethical and stable alternative to conventional finance. In various countries, both within the Muslim world and in non-Muslim countries, Islamic finance is recognized for its principles focused on justice, equity, and sustainability.

Products such as *sukuk* (Islamic bonds) and *ijarah* (lease contracts) have attracted the attention of not only Muslim investors but also international investors seeking more sustainable and ethical financial instruments. With significant growth, Islamic finance continues to play a key role in promoting financial inclusion and fostering a more equitable and stable economic development worldwide (Islamic Finance Development Report: Thomson Reuters & IFSB, 2023).

B. Basic Principles of Islamic Finance

Islamic finance is based on a set of principles that govern every financial transaction to ensure compliance with Sharia law. These principles not only serve as a legal framework but also as ethical guidelines that ensure justice, transparency, and economic sustainability. The principles include:

1. The first and most fundamental principle in Islamic finance is the prohibition of riba or interest. In Islam, *riba* is defined as an addition to the principal loan amount that must be paid by the borrower. The Qur'an explicitly forbids *riba* because it is considered unjust, where the borrower is burdened with additional costs without any risk or effort from the lender. Islamic finance proposes alternative models based on profit and risk-sharing, such as *mudharabah* and *musharakah*, where profits are distributed according to the contribution of capital and risk (Iqbal, Z., & Mirakhor, A., 2020).

2. The second principle is the prohibition of *gharar*, which means uncertainty or excessive speculation in a transaction. In financial transactions, *gharar* is prohibited because it creates uncertainty that may harm one party.

For example, transactions where essential information such as price, quality, or quantity of goods is not fully disclosed are examples of *gharar*. Islam encourages clarity and transparency in every financial transaction. Therefore, contracts containing uncertainty or ambiguity are not allowed. This helps protect all parties involved from harmful speculative risks (Iqbal, Z., & Mirakhor, A., 2020).

3. The third principle is the prohibition of *maysir*. The principle of *maysir* or gambling is also forbidden in Islamic finance. *Maysir* refers to activities that rely purely on chance or luck, such as gambling or speculative transactions. In finance, this prohibition applies to activities that do not add value to the economy, such as trading in derivatives based purely on price speculation without any real underlying assets. Islamic finance promotes investment in productive and real economic activities, such as investment in infrastructure projects, small and medium enterprises, or properties with clear economic benefits. This principle ensures that all transactions contribute to economic and social welfare (Iqbal, Z., & Mirakhor, A., 2020).

4. The fourth principle in Islamic finance is the asset-based principle. In Islam, all financial transactions must be supported by real assets or productive economic activities. This differs from conventional finance, which often trades in derivative financial products without any physical asset backing. For example, in Islamic finance, instruments such as *sukuk* (Islamic bonds) must be backed by ownership of real assets. *Sukuk* investors not only purchase the right to receive payments but also own a share of the underlying asset. This principle ensures that economic activities are real and not speculative.

5. The fifth principle is the principle of justice and equality, which is an important foundation in Islamic finance. Every transaction must be conducted fairly and must not harm any party. Contracts in Islamic finance, such as *ijarah* (leasing contracts), provide balanced rights and obligations between the lessee and the asset owner. This ensures that no party is exploited or harmed in the transaction. This justice is reflected in the concept of profit and loss sharing proportionally according to each party's contribution. The principle of justice is also evident in the prohibition of monopolies or price manipulation in the economy (Ayub, M., 2019).

6. The sixth principle is the prohibition of investment in non-halal businesses. In Islamic finance, investments must comply with Sharia principles, which prohibit investments in certain sectors such as alcohol, gambling, and the production or distribution of haram products. This means that Islamic investors must ensure that their funds are not used to support businesses considered unethical or contrary to Islamic teachings (El-Gamal, M. A., 2021). This prohibition reflects Islamic finance's commitment to moral and ethical integrity in all aspects of the economy. Additionally, it ensures that investments are not only financially profitable but also provide a positive impact on society.

7. The seventh principle is the profit-sharing principle, which is one of the main pillars of Islamic finance. Unlike the conventional financial system, which focuses on fixed returns like interest, Islamic finance promotes partnership-based models where profits and losses are shared based

on the contribution of capital and effort. In a *mudharabah* contract, for instance, one party provides capital, while the other provides labor and expertise. Both parties share profits according to an agreed ratio. In *musharakah*, all parties contribute capital and effort and share risks and profits proportionally. This principle ensures a fairer distribution of wealth and encourages productive economic cooperation (Hassan, M. K., & Lewis, M. K., 2022).

C. Islamic Financial Instruments

Islamic financial instruments are financial tools developed to facilitate financial transactions in accordance with Sharia principles. These instruments are designed to comply with prohibitions against *riba* (interest), *gharar* (uncertainty), and *maysir* (gambling), which are key pillars of Islamic finance. Moreover, Islamic financial instruments must be asset-based and support productive economic activities. In recent decades, these instruments have expanded significantly, with a wide range of products offered by Islamic banks, financial institutions, and capital markets worldwide, both in Muslim-majority and non-Muslim countries.

One of the most popular Islamic financial instruments is *sukuk*, often referred to as Islamic bonds. Sukuk is an asset-based instrument that grants investors ownership rights to the underlying assets. Unlike conventional bonds, which are debt-based, *sukuk* involves the ownership of real assets and the sharing of profits generated by those assets' productivity. There are several types of *sukuk*, including *sukuk ijarah* (asset lease-based), *sukuk mudharabah* (profit-sharing-based), and *sukuk musharakah* (partnership-based). *Sukuk* has been widely used by governments and corporations to finance infrastructure projects, property development, and energy projects in line with Sharia principles (El-Gamal, M. A, 2021).

Another important instrument in Islamic finance is *mudharabah*, a partnership agreement between the capital provider (*rabbul mal/shahibul mal*) and the business manager (*mudharib*). In *mudharabah*, the investor provides the capital, while the manager is responsible for running the business. Profits are shared according to a pre-agreed ratio, while losses are borne solely by the investor unless they result from the manager's negligence or misconduct. *Mudharabah* is commonly used to finance small and medium-sized enterprises (SMEs) that need capital but lack access to interest-based loans. This model emphasizes cooperation between those with capital and expertise (Ayub, M, 2019).

In addition to *mudharabah*, the *musharakah* instrument is also significant in Islamic finance. *Musharakah* is a partnership contract where two or more parties contribute capital to a specific project or venture, sharing profits and losses proportionally to their capital contributions. *Musharakah* is often used in financing large projects, such as infrastructure development, real estate, and energy projects. Unlike *mudharabah*, in *musharakah*, all parties involved not only share profits but also bear losses proportionally, reflecting the fair risk-sharing principle and avoiding exploitation (Ayub, M, 2019).

The *ijarah* instrument is similar to a leasing contract in conventional systems. In ijarah, the asset owner (lessor) leases the asset to the lessee for a specified period with agreed-upon rental payments. At the end of the lease period, the asset can either be returned to the owner or purchased by the lessee through *ijarah muntahia bittamlik* (lease ending with ownership). *Ijarah* is commonly used to finance vehicles, industrial equipment, and properties. One of *ijarah*'s key advantages is its flexibility, allowing the lessee to use the asset without purchasing or owning it outright (Hassan, M. K., & Lewis, M. K, 2022).

Murabahah is one of the most commonly used Islamic financial instruments in Islamic banking. *Murabahah* is a sales contract where the bank purchases an asset on behalf of a customer and then resells it to the customer at a profit margin agreed upon upfront. The customer repays this price in installments over time. The bank's profit is derived not from interest but from the margin on the sale of the asset. *Murabahah* is frequently used to finance homes, vehicles, and other consumer needs. Its transparency and clear agreement upfront make *murabahah* compatible with Sharia, which prohibits *gharar* (uncertainty) (Iqbal, Z., & Mirakhor, A, 2020). In addition, the *wakalah* instrument is another key aspect of Islamic finance. *Wakalah* is an agreement in which one party (*wakil*) is authorized by another party (*muwakkil*) to act on their behalf in specific economic activities. In Islamic finance, *wakalah* is often used in fund management, where financial institutions act as agents managing investors' funds in exchange for a fee. This instrument allows customers to delegate the management of their investments to experts in fund management (Hassan, M. K., & Lewis, M. K, 2022).

The diversity of Islamic financial instruments shows that the Sharia-compliant financial system goes beyond banking and includes capital markets, investment, and project financing. By adhering to sharia principles, these instruments provide ethical and sustainable alternatives for investors, governments, and corporations (Obaidullah, M, 2020). The use of Islamic financial instruments continues to grow in various countries, creating a more inclusive and equitable financial market. Innovations in Islamic finance, such as Islamic fintech, also open new opportunities for the advancement of sharia-compliant finance in the digital era (Hassan, M. K., & Lewis, M. K, 2022).

D. Global Development of Islamic Finance

Islamic finance has experienced rapid global growth in recent decades. Although initially dominated by Muslim-majority countries, the Sharia-compliant financial system has now expanded to non-Muslim countries, particularly in Europe, Asia, and North America. This growth is driven by increasing demand for financial products aligned with sharia principles, such as the prohibition of *riba* (interest), *gharar* (uncertainty), and *maysir* (gambling), as well as the rising interest in ethical and sustainable investments. International institutions such as the World Bank and the International Monetary Fund (IMF) have also begun to focus more on Islamic finance as part of a more inclusive and stable global financial system. Today, Islamic finance covers various sectors, including banking, insurance (takaful), and Sharia-compliant capital markets such as sukuk and Islamic equity (Usmani, M. T., 2021).

One of the key milestones in the global development of Islamic finance has been the rapid growth of *sukuk* (Islamic bonds). *Sukuk* has become an essential tool for governments and corporations to raise funds for infrastructure, property, and energy development projects (Obaidullah, M., 2020). Countries like Malaysia, the United Arab Emirates, Saudi Arabia, and Qatar have led the way in *sukuk* issuance, but recently, non-Muslim countries such as the United Kingdom, Hong Kong, and South Africa have also entered the global *sukuk* market. The global sukuk market has expanded rapidly, with total issuances reaching trillions of dollars. *Sukuk's* popularity in various countries highlights its appeal as a stable, transparent, and Sharia-compliant instrument (Hassan, M. K., & Lewis, M. K., 2022).

Islamic banking also plays a key role in the global development of Islamic finance. Since the establishment of the first Islamic bank in Dubai in 1975, the sector has grown significantly, with over 500 Islamic banks operating in more than 80 countries today. These banks offer a range of products and services that comply with Islamic principles, including *murabahah* (cost-plus financing), *ijarah* (leasing), *mudharabah* (profit-sharing), and *musharakah* (partnership). In countries like Malaysia, Saudi Arabia, and the United Arab Emirates, Islamic banking has become an integral part of the national financial systems. Outside the Islamic world, countries such as the United Kingdom and Germany are also developing Islamic banking sectors to attract investments from both Muslim and non-Muslim communities seeking ethical financial products (Obaidullah, M., 2020).

Takaful, the Sharia-compliant version of insurance, has also emerged as an important sector within global Islamic finance. The concept of *takaful* is based on the principle of mutual risk-sharing and solidarity among participants. Unlike conventional insurance, which operates on a profit-based model, *takaful* collects contributions from participants into a common pool used to cover claims from other participants. The *takaful* industry has grown rapidly in the Middle East and Southeast Asia, particularly in Malaysia and Indonesia. Other countries, such as Sudan and Bahrain, have also developed their *takaful* industries. *Takaful* products include not only life and health insurance but also vehicle, property, and commercial insurance (Ayub, M., 2019).

In addition, the Islamic capital market has grown significantly, particularly in countries with dual legal systems, such as Malaysia. Sharia-compliant equities are a key component of the Islamic capital market, where stocks that adhere to Islamic principles are traded. Halal stocks must not be involved in businesses prohibited by Sharia, such as alcohol, gambling, *riba* (interest-based activities), or other *haram* industries. Institutions such as the Dow Jones Islamic Market Index (DJIM) and the FTSE Shariah Index have helped promote the growth of the Islamic capital market by providing guidelines for investors on Sharia-compliant stocks. Stock exchanges in countries like Malaysia, Saudi Arabia, and Indonesia have also developed special trading platforms for Islamic equities (Usmani, M. T., 2021).

Beyond the capital markets and banking, the development of financial technology (fintech) within Islamic finance, or Islamic fintech, has become a recent trend in the global Islamic finance landscape. Sharia-compliant fintech offers digital solutions that make it easier to access Sharia-compliant financial services, including payments, financing, and investments. In Indonesia and Malaysia, Islamic fintech is growing rapidly, with various startups offering Sharia-compliant lending services, crowdfunding platforms, and Sharia-compliant e-wallets. This technology provides faster and easier access to financial services for communities not yet reached by traditional Islamic banking, thereby promoting greater financial inclusion (Obaidullah, M, 2020).

However, despite the rapid growth of Islamic finance, several challenges remain in achieving its full potential globally. One of the main challenges is the lack of standardization in Sharia financial regulations and practices across different countries. Differences in Sharia interpretation and the lack of regulatory harmonization between jurisdictions can hinder the sector's growth. Additionally, the shortage of skilled and knowledgeable human resources in Islamic finance poses a limitation in some countries. Nevertheless, Islamic finance continues to show great potential as an ethical, inclusive, and sustainable financial system for the future (Khan, M. F., & Bhatti, M. I., 2021).

E. The Future of Islamic Finance: Innovation and Challenges

Islamic finance continues to grow globally and is expected to play an increasingly important role in the future economic system. This financial system is based on Sharia principles that emphasize justice, balance, and transparency in economic transactions. With the rising interest in ethical and sustainable financial products, Islamic finance has the potential to become a more inclusive alternative compared to conventional financial systems (Chapra, M. U., 2019). However, to reach its full potential, the future of Islamic finance must adapt to global trends, adopt technological innovations, and address various challenges, both in terms of regulation and implementation.

1. Technological Innovation in Islamic Finance

Technological advancements, particularly in the field of fintech (financial technology), have transformed the global financial landscape, including Islamic finance. Digital technology allows broader access to Sharia-compliant financial products and creates a more inclusive ecosystem for communities previously underserved by traditional banking services. Islamic fintech, which combines Islamic financial principles with modern technology, enables more efficient, transparent, and secure transactions. Products such as Sharia-compliant crowdfunding, peer-to-peer (P2P) financing, and Sharia-compliant e-wallets are becoming increasingly popular, especially in countries like Malaysia and Indonesia, which are hubs for Islamic fintech innovation. In the future, technologies such as blockchain and smart contracts could also be integrated into Islamic finance systems to create more efficient and transparent transactions while ensuring Sharia compliance (Obaidullah, M, 2020).

2. **Green Finance and Sustainable Finance**

In the future, Islamic finance is expected to become more integrated with green finance or sustainable finance initiatives. The principles of Islamic finance, which emphasize social justice, environmental protection, and the prohibition of speculative activities, align well with the sustainability goals pursued by the global community. For instance, instruments like green *sukuk* have been introduced as a way to finance environmentally friendly projects that comply with Sharia principles. Green *sukuk* are used to fund sustainable infrastructure projects, renewable energy, and environmental conservation efforts. Countries like Malaysia and Indonesia have led the issuance of green *sukuk*, and this market has significant growth potential as global demand for ethical and sustainable investments increases (Obaidullah, M., 2020).

3. **Global Standardization of Islamic Finance**

One of the main challenges facing Islamic finance today is the lack of standardization in the regulation and implementation of Sharia-compliant financial products across different countries. Variations in Sharia interpretation and legal practices across jurisdictions often create gaps in the application of Islamic financial products. To address this challenge in the future, it is essential for international organizations such as the Islamic Financial Services Board (IFSB) and the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) to strengthen efforts toward regulatory harmonization and standardization of Sharia-compliant financial products. With clearer and more uniform standards, Islamic finance will become more widely accepted and accessible to the global community, creating a more transparent and reliable system (Obaidullah, M., 2020).

4. **Financial Inclusion and the Role of Islamic Finance**
   Islamic finance has great potential to expand financial inclusion, particularly in countries with large Muslim populations that are underserved by conventional banking systems. Sharia-compliant financial institutions can play a vital role in providing access to banking and financial services to communities that previously lacked such access. Instruments such as Sharia-compliant microfinance, *zakat*, and *waqf* hold strategic importance in reducing poverty and improving social welfare in various countries. In the future, with better integration of technology and improved regulation, Islamic finance can become a stronger tool for achieving global financial inclusion, providing broader access to financial resources for individuals and small and medium-sized enterprises (SMEs) (Obaidullah, M., 2020).

5. **Human Resource Development and Islamic Finance Education**
   To ensure the sustainability and growth of Islamic finance in the future, the development of human resources and capacity building in this sector is crucial. Islamic finance education must be expanded and enhanced to produce professionals with a deep understanding of Sharia principles and the dynamics of global financial markets. Several universities and educational institutions around the

world have offered specialized programs in Islamic finance, but in the future, greater efforts are needed to make this education more affordable and accessible. Additionally, collaboration between educational institutions, governments, and the private sector will be key to developing the talent needed to support the growth of Islamic finance globally (Obaidullah, M., 2020).

6. **Regulatory Challenges and Sharia Compliance**
   Although Islamic finance continues to grow, regulatory challenges and Sharia compliance remain significant issues to address. Every Islamic financial product must undergo a strict Sharia audit process to ensure compliance with Islamic principles. In the future, there needs to be an enhancement in the capacity of Sharia supervisory bodies to ensure that Islamic financial products and services remain compliant with Islamic teachings while adapting to changing market conditions. International collaboration between regulators, central banks, and Islamic financial institutions will be crucial in creating a stronger regulatory framework that supports innovation without compromising Sharia compliance (Obaidullah, M., 2020).

7. **Market Potential and Global Growth of Islamic Finance**
   Islamic finance holds tremendous potential for continued growth in the future, especially with increasing interest in ethical and sustainable investments. In Muslim-majority countries, such as those in the Middle East and Southeast Asia, Islamic finance has become an integral part of the economic system. However, Islamic finance has also started to gain interest in non-Muslim countries, particularly in Europe and North America, where Sharia-compliant financial products are seen as an ethical investment

alternative. With a growing market and increasing demand, Islamic finance in the future has the potential to become one of the main pillars of the global financial system, contributing to economic stability and social justice (Warde, I., 2020).

F. Conclusion

Islamic finance is built on a solid foundation based on sharia principles that prioritize justice, transparency, and ethics in transactions. The prohibitions against *riba* (interest), *gharar* (uncertainty), and *maysir* (gambling), along with a commitment to risk and profit-sharing, are the main pillars that distinguish Islamic finance from conventional financial systems. In the future, Islamic finance has the potential for significant growth, driven by technological innovations, including sharia fintech, as well as integration with the increasingly popular concept of green finance.

Despite challenges related to regulation and standardization, as well as the need for human resource development, Islamic finance demonstrates an ability to adapt to changing times. Involvement from educational institutions, regulators, and the industry is crucial in creating a framework that supports the sustainability and integrity of Islamic finance. With the right support, Islamic finance can not only enhance financial inclusion in majority Muslim countries but also provide more ethical and sustainable financial solutions for a broader global market.

Thus, Islamic finance has the potential to serve as a key pillar in a more stable, inclusive, and just global financial system, making a significant contribution to economic growth and social welfare worldwide.

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ISLAMIC BANKING PRACTICES

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A. Introduction

Indonesia as one of the countries with potential in the development of Islamic economics and finance. Based on the State of The Global Islamic Economy Report in 2023, Indonesia is ranked third in the world after Malaysia and Saudi Arabia. This result is in line with Indonesian Islamic finance also recorded an achievement in third place based on the Islamic Finance Development Indicator Report in 2023. The main indicators that contributed to this achievement are in terms of science and research for the development of Islamic finance. In the report, Indonesia received the highest score reflecting support from stakeholders, through the preparation of applicable research in supporting the acceleration of national Islamic financial development.

The development of Islamic finance in Indonesia based on its assets reached 2,582.25 trillion, with the market share of Islamic finance in 2023 reaching 10.95 percent. Islamic banking is one of the rapidly growing Islamic financial industries in Indonesia. Indonesia is one of the countries that adopts a dual banking system. Where Islamic banking and conventional banking run side by side. The market share of Islamic banking in Indonesia based on the report on the development of Indonesian Islamic finance in 2023 reached 7.44 percent. Islamic banking assets amounted to 892.17 trillion.

The government in order to support the development and strengthening of Islamic banking and other Islamic financial industries by issuing the Roadmap for the development and strengthening of Indonesian Islamic banking 2023-2027. Islamic banking is stated to face opportunities and challenges in its development. Challenges in its development include differentiation of business models, quality of human resources and IT, size and capitalization, public understanding. On the other hand, Islamic banking has potential opportunities including in terms of the uniqueness of Islamic products, business orientation and public welfare, economic growth in the halal industry, potential for managing social funds.

B. Islamic Banking Operations

Islamic Banking according to Law Number 21 of 2008, is something related to Islamic Banks and Islamic Business Units, including institutions, business activities and methods and processes in carrying out its business activities. A bank is a business entity that collects funds from the public in the form of savings and distributes them to the public in the form of credit and/or other forms in order to improve the standard of living of the people.

Islamic Bank is a Bank that carries out its business activities based on Sharia Principles. Islamic Banks are divided into Islamic Commercial Banks, Islamic Business Units and Islamic People's Economic Banks. Islamic Banking Assets are growing. The following is the development of Islamic Banking Assets.

Table 1.
Islamic Banking Assets (trillions)

	2019	2020	2021	2022	2023
BUS	350,36	397,07	441,79	531,86	594,71
UUS	174,20	196,88	234,95	250,24	274,28
BPRS	13,76	14,49	17,06	20,16	23,18
Total	538,32	608,89	693,80	802,26	892,17

Source: Islamic Banking Statistics

Table 2.
Key Indicators for Islamic Banking

	Number of Institutions	Number of Offices	Assets (trillions)	Financing (trillions)	DPK (trillions)
BUS	13	1.967	594,71	368,38	465,93
UUS	20	426	274,28	200,06	203,32
BPRS	173	693	23,18	17,03	15,27
Total	206	3.086	892,17	585,46	684,52

Source: Islamic Banking Statistics, 2023

Table 2 above is a table of the main performance indicators of Islamic banking in 2023. The information presented consists of the number of institutions, number of offices, assets, financing and DPK based on the bank category. BPRS has the largest number of institutions, namely 173 with 3,086 offices. Based on its assets, the highest is BUS, namely 594.71 trillion. Based on third-party funds collected by the bank, the highest is BUS, reaching 465.93 trillion.

C. Digital Resilience of Islamic Banking

The rapid development of information technology requires banks to accelerate digital transformation. Digitalization provides benefits to increase efficiency in various aspects. However, digitalization also presents a number of challenges and risks for banking that need to be anticipated and mitigated. The Financial Services Authority in order to mitigate the challenges and risks in the utilization of digitalization in the banking sector issued a digital resilience guide.

Resilience is defined as a process to utilize existing resources to maintain business continuity, where the application of this concept is in terms of technology and the internet in the current digital era. Digital resilience focuses on the overall ability of the organization to adapt to the digital environment quickly, including cybersecurity, shifting consumer expectations, regulatory changes, technological advances, including having the flexibility and agility to respond to change and find new opportunities to be able to maintain business.

In order to implement digital resilience, Banks can refer to the Digital Resilience Framework. The framework consists of three main aspects, namely resilience to business dynamics, bank resilience to disruption, and customer resilience in the digital era.

1. **Resilience to Business Dynamics (Digital Competitiveness)**

   The bank's ability to survive in the dynamics of digital era business so that the bank's business remains relevant in the market. In order to maintain the bank's digital competitiveness which includes three things, namely technology adoption, human resources and organizations in the digital era, and consumer-oriented product development.

   a. **Technology Adoption**

      The choice of bank technology is a factor that influences the competitiveness of bank business because it will determine what products and services the bank can provide, as well as the ecosystem that the bank can enter. In technology adoption, there are several factors that need to be considered. In general, the factors in question can be divided into four clusters, namely: financing and supporting resources, expertise and knowledge, organizational culture, and regulation.

   b. **People and Organization**

      It requires human resources and organizational structures that are able to adapt to the dynamic development of technology and business. With the support of adequate human resources and organizational structures, banks can survive in the business competition of the digital era through innovation and implementation of technology.

   c. **Customer Centric Product Development**

      Banks need to provide products and services that are in accordance with consumer needs or achieve customer centric orientation services. This is done by considering four things, namely customer engagement, customer experience, customer insight and customer trust and perception.

2. Bank Resilience to Disruption in the Digital Landscape

This aspect is divided into three stages, namely anticipate, withstand and recover and sustain.

a. Anticipate

Banks at this stage anticipate disruptions through the implementation of the Business Continuity Management (BCM) framework. BCM is a series of practices that include the implementation of policies, standards, processes, and steps to maintain the Bank's function during operational disruptions.

b. Withstand and Recover

Bank at the withstand and recover stage is a process that describes the Bank's ability to continue operating effectively during a security incident or disruption along with the execution of procedures and policies to handle the disruption. This stage focuses on managing the impact of the attack and restoring critical systems and functions to normal after the disruption.

c. Sustain

The Bank at the sustain stage is a stage where the Bank carries out evaluation and development to improve the Bank's capabilities and knowledge of the disruptions that have occurred as an effort to develop better resilience procedures and minimize the impact of future disruptions.

3. Customer Resilience in the Digital Era

To increase consumer resilience, Banks need to implement policies in the form of:

a. Customer Incident Management

A series of policies/mechanisms by the Bank that aim to provide consumers with an understanding of the risks when doing activities in the digital space and to be aware when they are at risk/under digital attack. as an anticipatory step against digital attacks aimed at consumers.

To increase consumer resilience to digital attacks, the Bank can take the following steps: first, educate and socialize consumers about the types of risks when in the digital space and how to manage these risks. Second, provide an understanding of positive internet usage, actions that can threaten personal data leakage, and the obligation to protect personal information such as OTP, PIN, and password. Third, have an adequate supporting ecosystem such as policies and procedures related to reporting mechanisms for consumers who experience digital attacks. Fourth, dedicated reporting channels for consumers to report fraud and online fraud, conduct inventory and update fraud and scam data, and coordinate with authorities and law enforcement for law enforcement purposes. Fifth, user-friendly reporting services and formats according to the age of the consumer.

b. Customer Incident Recovery

A series of policies/procedures that aim to provide clear guidance and mechanisms to consumers on how consumers should act when they experience risks in the digital space or receive digital attacks. as a step to overcome digital incidents/attacks experienced by consumers and their recovery strategies.

In order to help consumers deal with digital attacks, Banks can take the following steps: first, provide guidance and support to consumers on how to act/respond to digital attacks. Second, Provide further guidance to consumers on which parties need to be contacted regarding the attacks/risks faced and guide consumers to report incidents experienced to law enforcement authorities. Third, Provide assistance and assistance to consumers who experience digital attacks with significant losses.

c. Customer Post-Recovery Services

Consumer support services that aim to provide education on digital risks/attacks experienced by consumers and help consumers be more careful not to repeat previous mistakes so that consumers can avoid digital attacks in the future. As an effort to evaluate digital attacks that occur to consumers and steps so that consumers do not experience similar attacks in the future.

Banks can make several efforts as follows, first, Provide information services for consumers to increase their knowledge/ability to use online applications/services to anticipate if consumers experience online attacks/threats in the future. Second, Provide assistance to consumers who have experienced digital attacks and report to the bank, through periodic notifications/reminders regarding the dangers/risks in the digital space and the need for vigilance in digital transactions. Third, the Bank recapitulates the results of reports made by consumers regarding digital attacks experienced and evaluates and prepares education and socialization strategies based on the results of the report analysis so that consumers can avoid similar attacks in the future.

D. Development and Strengthening of Islamic Banking

In order to support a resilient economy, the government issued Law Number 4 of 2023 concerning the development and strengthening of the financial sector. The Financial Services Authority, along with the issuance of the Law, prepared a Roadmap for the development and strengthening of Indonesian Islamic banking 2023-2027. The Roadmap was prepared to strengthen the policy for the development and strengthening of national Islamic banking. The transformation of Islamic banking is the main focus to bring this industry towards a stronger and more competitive Islamic banking, and to contribute significantly to the national economy and social development.

The five main pillars of the Policy Direction, namely Strengthening the Structure and Resilience of the Islamic Banking Industry, Accelerating the Digitalization of Islamic Banking, Strengthening the Characteristics of Islamic Banking, Increasing the Contribution of Islamic Banking to the National Economy, and Strengthening the Regulation, Licensing, and Supervision of Islamic Banking. All of these pillars are a strong foundation for a more resilient and sustainable Islamic banking.

1. Pillar 1 – Strengthening the Structure and Resilience of the Islamic Banking Industry

Strengthening the structure and resilience of the Islamic banking industry is expected to be achieved through the following strategies.

a. Consolidation of Islamic Banks
   The planned work program is the consolidation of Islamic Banks to increase competitiveness through the fulfillment of core capital, mergers, acquisitions, Bank Business Groups. The expected end result is the formation of BUS with large-scale assets and the formation of a strong BPRS.

b. Strengthening Islamic Business Units through spin-off policies
   The planned work program is the Development and Strengthening of Islamic Business Units through spin-off policies and consolidation of Islamic Business Units. The expected final result is the issuance of the OJK Islamic Business Units Regulation, the separation process runs well and the formation of strong Islamic Commercial Banks resulting from the spin-off and all Islamic Business Units have a minimum business fund of IDR 1 trillion according to the OJK Islamic Business Units Regulation.

c. Increasing the efficiency of Islamic banking through synergy with the main bank
   The planned work program is the optimization of synergy between Islamic banks and the integration of services owned by the Parent Bank. The expected end result is the addition of the number of business activities, services, and operational banking synergies, increasing the efficiency of Islamic Commercial Banks and improving the quality of standardized Islamic banking services with the main bank.

2. **Pillar 2 – Accelerating the Digitalization of Islamic Banking**

Acceleration of digitalization of Islamic banking is expected to be achieved through the following strategies.

a. Implementation and sustainability of Islamic banking Information Technology (IT)

The planned work program is to encourage the digitalization of Islamic Commercial Banks through the Fulfillment of IT Provisions for Islamic Commercial Banks. The expected end result is the Fulfillment/adequacy of the implementation of IT Provisions for Islamic Commercial Banks according to the provisions.

b. Development of IT modules according to the characteristics of Islamic banking products

The planned work program is the development of funding and financing modules that are in accordance with the characteristics of Islamic banking products. The expected end result is the availability of guidelines for the development of Islamic banking IT, there is an increase in the number of Islamic banks that have IT modules according to the characteristics of Islamic banking products.

c. Acceleration of digitalization of Islamic Banking services

The planned work programs are first, the implementation and monitoring of IT in accordance with the Digital Service Provisions. second, encouraging the digitalization of BPRS services. The expected end result is an increase in the number of banks cooperating with IT Service Providers, there are BPRS Cooperation Guidelines with Fintech P2P Financing and increased implementation of digitalization in BPRS business processes.

3. **Pillar 3 – Strengthening the Characteristics of Islamic Banking**

   Strengthening the Characteristics of Islamic Banking is expected to be achieved through the following strategies.

   a. Strengthening Shari'ah Governance Framework
      The planned work program is the optimization of sharia governance in Islamic Banking through sharia governance provisions and the establishment of the Sharia Finance Development Committee. The expected end result is the implementation of sharia governance in Islamic Banking in accordance with the provisions, the formation of the Sharia Finance Development Committee and recommendations from the Sharia Finance Development Committee.

   b. Development of unique sharia products
      The planned work program is first, the preparation of sharia banking product guidelines. Second, the development and implementation of unique sharia banking products. The expected end result is the existence of 10 Islamic Banking Product Guidelines and an increase in the portfolio of unique Islamic banking products (Salam, Ishtisna', SRIA, CWLD).

   c. Strengthening the role of Islamic banking in sustainable finance
      The planned work program is the implementation of sustainable finance in Islamic banks in order to support sustainable development. The expected end result is a

Sustainable Finance Series Book for Islamic Banking and an increase in the financing portfolio for sustainable projects.

d. Rebranding of Islamic banking
The planned work program is to encourage increased inclusiveness of Islamic banking. The expected end result is that there is an Islamic Banking Rebranding Guide and acceleration of increasing the market share of Islamic banking.

e. Improving the quality of Human Resources (HR) that reflects Islamic values.
The planned work program is first, guidelines for the Islamic Banker Code of Ethics. Second, encouraging the preparation of Islamic banker competency standards. The expected end result is guidelines for the Islamic Banker Code of Ethics, the issuance of the KKNI General Banking which includes the DPS level and the fulfillment of the number/percentage of HR in Islamic banking that has been certified.

4. Pillar 4 – Increasing the Contribution of Islamic Banking to the National Economy

Increasing the contribution of Islamic banking to the national economy is expected to be achieved through the following strategies.

a. Increasing literacy and inclusion of Islamic banking
The planned work program is Increasing literacy and inclusion through synergy with stakeholders of the Islamic ecosystem. The expected end result is Increasing the level of literacy and inclusion of Islamic banking.

b. Strengthening the role of Islamic banking in the Islamic economic ecosystem
   The planned work programs are first, increasing awareness of Islamic finance through national and international seminars. Second, expanding access to Islamic banking services in the Islamic economic ecosystem, including synergy with other Islamic Financial Services Institutions, the Government, and the halal industry. The expected end result is increased synergy between Islamic banking in the Islamic economic ecosystem and increased accumulation of transaction value in Islamic banking.

c. Increasing the role of Islamic banking in the MSME sector
   The planned work programs are first, increasing access and assistance to Islamic banking in the unbankable MSME sector through Islamic social financial instruments (ZISWAF, charity funds, CSR). Second, increasing access to KUR and commercial financing for MSMEs. The expected end result is that there are several Islamic banks that empower unbankable MSMEs through Islamic social financial instruments and there is an increase in access to financing for MSMEs.

d. Strengthening the implementation of consumer and community protection in the Islamic banking industry
   The planned work program is Optimizing the implementation of consumer and community protection carried out by the Islamic banking industry. The expected end result is an increase in the level of compliance of Islamic banking with the implementation of consumer and community protection principles.

5. **Pillar 5 – Strengthening Regulation, Licensing, and Supervision of Islamic Banking**

   Strengthening regulation, licensing, and supervision of Islamic banking is expected to be achieved through the following strategies.

   a. Acceleration of licensing process and strengthening of integrated licensing

      The planned work program is IT Development to support the acceleration of the process and strengthening of integrated licensing. The expected end result is automation and simplification of integrated and cross-sectoral licensing processes and harmonization of integrated sharia licensing documents and processes.

   b. Regulations that are oriented towards resilience, competitiveness and socio-economic impacts, by taking into account best practices and/or international standards

      The planned work program is first, the preparation of provisions that prioritize the development and strengthening of Islamic banking. Second, Alignment of provisions with the development of best practices and/or international standards. The expected end result is a policy that supports the development and strengthening of Islamic banking, OJK provisions that are in line with the development of best practices and/or international standards.

   c. Technology based supervision for early detection and maintaining the integrity of the banking system

      The planned work program is the evaluation and development of the methodology, process and coordination mechanism of Islamic bank supervision and integrated supervision of technology-based financial conglomerates. The expected final result is Internal provisions related to the methodology, process and coordination mechanism of Islamic banking supervision, as well as the development of an Islamic banking information system.

d. Industrial development through cooperation with international institutions to develop the industry sustainably
The planned work program is the coordination of technical assistance with IFSB or other international institutions for the development of Islamic banking. The expected end result is the implementation of technical assistance with IFSB or other international institutions. The implementation of workshops and/or capacity building of IFSB or other international institutions

In addition to the five pillars of the foundation for strengthening Islamic banking, the roadmap for the development and strengthening of Indonesian Islamic banking 2023-2027 mentions the supporting devices needed. These supporting devices include first, leadership and change management, second, infrastructure (technology and human resources), third, synergy and collaboration with stakeholders.

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ISLAMIC CAPITAL MARKET

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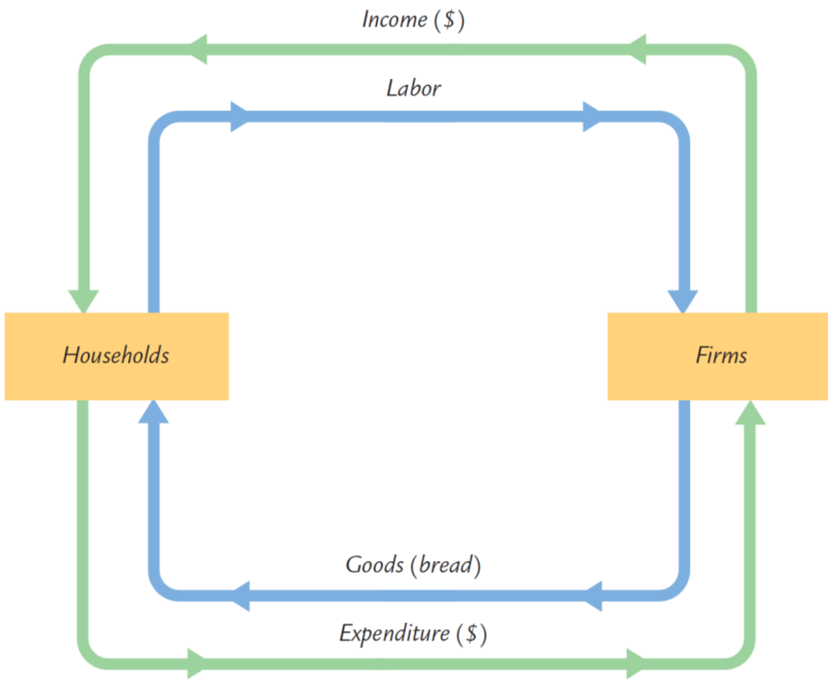
A. Introduction

In macro perspective, capital market is important part particularly in circular flow concept. In this concept, there are two flows. The first is the flow of real sector (production aspect), and the second one is the flow of monetary sector (money aspect). In this circular flow as depicted in image 1 below, economic agents are assumed just consists of firms and households. The inner loop (blue line) shows the flow of real sector where firms that produce goods need factors of production (Labor) provided by household.

Image1. Circular Flow Economy



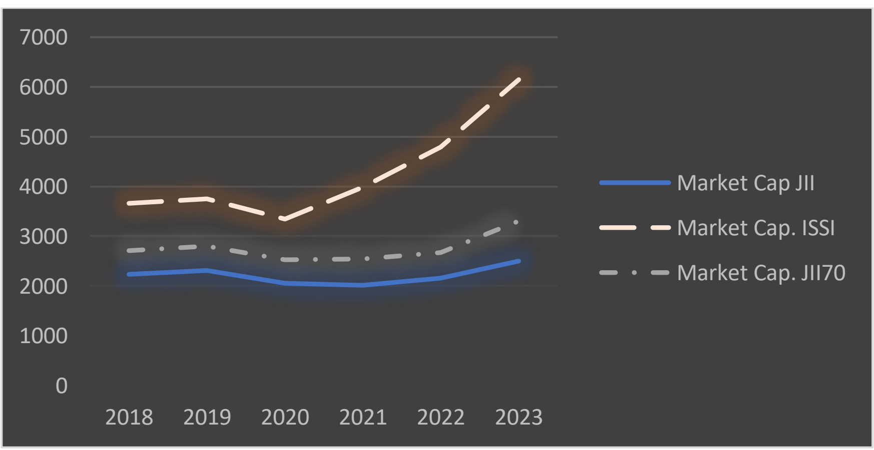
Source: Mankiw (2010), Macroeconomics

In the monetary aspect, firms will use labor to produce goods and the firms have to give returns to households in the forms of wages or income. This flow is delineated in the upper side of outer loop (green line). As labors has income, they will use it to buy good produced by firms (expenditure by household). This flow is delineated in the lower side of outer loop. This circular flow shows that income (Y) will exactly the same with expenditure (E), or Y = E. However, in reality, not all the gathered income is spent on purchases. There are some fractions of income that is held as saving. This saving is one form of economic leakage which need to be injected in the economy (in the circular flow system). Therefore, to provide this saving to be injected in economy, financial institutions are needed. One of it is capital market.

Mankiw (2013) explained that stock market as part of capital market product can depicts economic condition. This explanation is supported by several research such as Chang and Li (2024) that shows capital market volatility has impact on macroeconomic growth, Lyu, Wang and Zhang (2023) shows that the capital market opening affects to total level, quality and quantity of enterprise green innovation, and the effect on the total level and quality is greater than the quantity, and also study conducted by Oprea and Stoica (2018) who show that integration of capital market can affect economic growth.

In Indonesia, the demand for capital market that in line with the values and tenets of Islam is increasing. As shown in graph 1 below, market capitalization in Jakarta Islamic Index (JII), ISSI, and also JII70 show positive trend from 2018 to 2023. The highest market capitalization trend is ISSI (*Index Saham Syariah Indonesia*), followed by JII70 that is depicted by dash-dot line, and the last is JII.

Graph1. Market Capitalization in Islamic stock



Source: OJK Capital Market Fact book (2023, Processed)

In 2020, market capitalization of ISSI dropped by 10,68% from 3744,8 (in 2019) to 3344,9. The same pattern also occurs in JII and JII70 from 2019 to 2020. The former is dropped by 11,2% from 2318,5 to 2058,7, and the latter is dropped by 9,73% from 2800 to 2527,4. This decreasing pattern in Islamic Capital Market might show the effect of Covid 19 pandemic on investor decision to invest in Islamic capital market. The highest capitalization recorded for each index is all in 2023. ISSI is 6145,9; JII70 is 3306; and JII is 2501,4. These values might show the recovery process from the pandemic. However, these market capitalizations are lagging far behind IDX composite index, which recorded market capitalization of 11.665,94 (OJK Capital Market Fact Book, 2023).

As Islamic capital market is relatively a new product, then it is important to increase its development with hope in the long run at least Islamic capital market products can compete with the conventional one. One path that can be taken is by introducing Islamic capital markets. Therefore, this paper will introduce and describe about Islamic capital market, especially its products, and also highlights some issues related to Islamic capital market.

B. Theoretical Underpinning about Islamic Capital Market

Official website of OJK defines capital market based on the Law Number 8 of 1995, where Capital Markets (UUPM) governs activities related to Public Offerings and the trading of Securities, Public Companies in connection with the Securities they issue, as well as institutions and professions related to Securities. Based on this definition, Official website of OJK then defines Islamic capital market terminology as activities in the capital market as regulated by the Capital

Market Law (UUPM), which do not contradict Sharia principles.

Omar, Abduh, and Sukmana (2013) explained that the Islamic capital market is an integral part of the Islamic financial system. It plays an important role in complementing the investment role of the Islamic banking sector. Although its functions are similar with conventional capital markets, the way it is structured may be different from conventional ones (Omar, Abduh, and Sukmana, 2013).

Capital market deals with a commodity called capital (Krichene, 2013). Krichene (2013) then explained that transaction in capital market consists on the act of saving met by investment. Therefore, it involves an exchange of money as capital (saving) to be exchanged for securities (financial investment) such as bond, equity or *sukuk,* stock, an Islamic securitized asset.

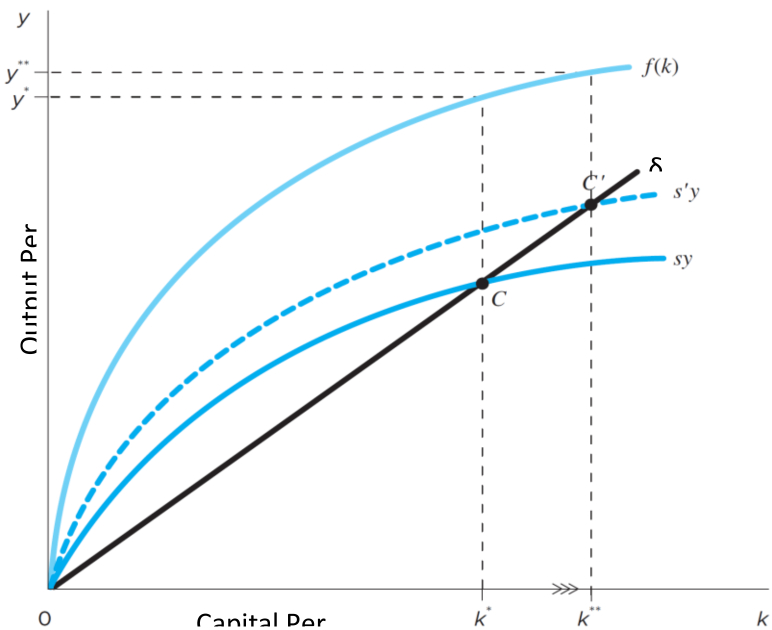
Theoretically, capital accumulation can impact to economic growth based on Solow growth model. In this model, explained by Mankiw (2013), supply of output per worker (y) is a function of capital per worker (k), or $y = f(k)$. this output per worker is demanded into two sectors of economy, viz consumption per worker (c) and investment per worker (I), or $y = c + I$. If consumption can be modelled by: $c = (1-s)y$ where s is saving rate, then the equation $y = c + I$, can be changed to : $y = (1-s)y + I$. The simplification of that equation gives $sy = I$.

Furthermore, as investment (I) is expenditure on new plant and equipment and it causes the capital stock to rise (Mankiw, 2013), depreciation leads the old capital stock to wear out and causes the capital stock to fall. Therefore, this explanation can be modelled as:

$\Delta k = I + \delta k$, where

Δk is the change in capital stock, and δk is depreciation of capital. As investment (I) is more than depreciation (δk), then capital will be accumulated overtime (Δk to rise). The increase of investment because the rate of saving is rising, as stated in this equation: sy = I that is explained before. as investment (I) is the same as depreciation (δk), this means that capital accumulation is zero. This condition is well-known as *steady state condition,* or I = δk. This whole basic Solow growth model explanation then can be graphed in this Graph 2. Below.

Graph 2. Solow Growth model



Source: Adopted from Dornbusch, Fischer, and Startz (2018)

Based on graph 2 above, as country save at a certain level, in the long run capital (k) accumulate as long as Investment (I = sy) is more than depreciation (δk). This condition will end when investment equals depreciation at point C above, with level of capital per worker at point k*. Therefore, at k*, the growth rate of output per worker (y) is called steady state growth rate that will be acquired in the long run. In addition, as explained by Dornbusch, Fischer, and Startz (2018), if a country wants to increase steady state growth rate from point C to C', then saving rate at certain level must be increased.

Based on this model, as saving from financial institution is invested to buy stock in primary market, or invested in obligation or *sukuk* released by government or private firms, this transaction will accumulate level of capital and will lead to a certain level of steady state growth rate of output in the long run. As level of saving that is invested increase, steady state growth rate will also increase in the long run.

C. Products in Islamic Capital Market

There are several products or instruments that can be categorized as product in capital market and also in money market. The key difference between these two are maturity date. In general, all instruments with less than a year in terms of maturity date are categorized as money market instruments, whereas those with more than a year are categorized as capital market instruments. Two well-known instruments in Islamic capital markets that will be described in this paper are Islamic equities and sukuk.

1. Islamic equities

Bacha and Mirakhor (2013) explained that equity financing has no fixity of return but has returns that are tied to the earning of the underlying business. As firms need to expands their business, one way to finance it is by issuing common stocks or shares. In many ways, this investment in stock resembles the provision of *Mudarabah* financing (Bacha and Mirakhor, 2013). However, Bacha and mirakhor (2013) further explained, because some companies might be involved in business that are *haram,* or kinds of activities which is prohibited, then not all stocks listed in an exchange may be acceptable from a sharia viewpoint.

Therefore, *sharia* evaluation is needed to categorize stocks of companies are *sharia*-compliant, or not. Based on Bacha and Mirakhor (2013), one layer of screening process to determine a firm is sharia-compliant or not is by seeing the line of business or core business the company. Company's core activities such as casino, conventional bank, the sale of alcohol and pork, others prohibited activities in Islam will be excluded. The second layer is by examining company's finance. Marzab (2011) described rule of thumb in determining sharia-compliant stock into two categories, viz asset-based rulebook, and market-capitalization rulebook. In asset based, the rule is as follows:

a. less than 5 % for non-permissible income / total income
b. less than 33 % for interest bearing debt/asset; receivables/asset and interest-bearing cash and investment / total asset.

Furthermore, for market -capitalization, the rules are: (1) interest-bearing debt/12-month average market capitalization; (2) receivables/12-month average market capitalization, and (3) interest-bearing cash and investment/12-month average market capitalization, all must less than 33%.

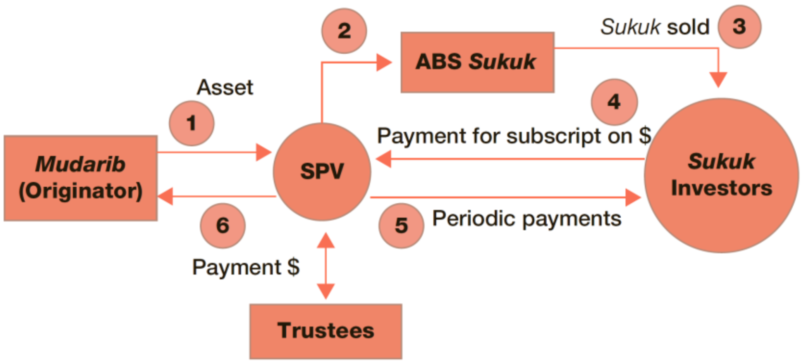
As companies meet all the requirement, then the stock can be categorized as *sharia*-compliant stock and will be re-examined, based on Bacha and Mirakhor (2013), at least every 6 months. The first stocks are traded first time in primary market. The result of this trading will increase capital of the firms and hopefully can be used to expand their business. In financial aspect, investors who do not get the stocks can buy them in secondary market.

2. Sukuk

Sukuk is the shari'ah alternative to the bond as practiced in the modern capital market (Billah, 2019). While the objective of a *sukuk* issuance may be the same as that of bond to raise financing, there are many differences between the two instruments (Bacha and Mirakhor, 2013), viz : (1) different from bond, all fund raised by sukuk must only be used for *halal* activities, (2) assets being financed should be identified because, differ from bond, *sukuk* cannot be used to fund general financial needs of issuers, (3) income received by investors are from cash flow generated from underlying asset, not from external parties, (4) *sukuk holders* have a right to own underlying asset and its cash flow, therefore there should be clear and transparent specification of right and obligation between *mudharib* and *sukuk* holders, (5) there should be no fixity in returns

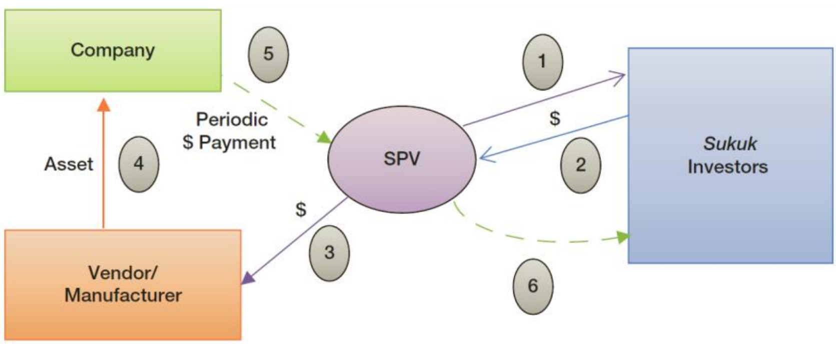
Bacha and Mirakhor (2013) explained that *Sukuk* are structured product, so their design would depend on several factors such as (1) compliance with underlying *sharia* contract, (2) risk profile, (3) the desired cash-flow, and potential market acceptance of the sukuk. Sukuk as structured product are explained in figure 1 and figure 2 below.

Figure1. Generic Asset-backed *sukuk* structure



Source: Bacha and Mirakhor (2013)

Figure 2. Typical *Ijarah*-based *sukuk* structure



Source: Bacha and Mirakhor (2013)

Figure 1 above is a generic asset-backed sukuk structure where *mudharib* or the issuer (borrower) must establish a legal entity called SPV (Special Purpose Vehicle). in point 1 figure 1, originator then injects or transfers assets that will become underlying asset for issuing *sukuk* certificate (point 2). Then the *sukuk* certificate can be sold in primary market to investors (point 3) and the investors make payment for subscription (point 4). The sukuk payments to investors are made by the SPV from the funds it receives from the *mudharib* (originator) in exchange for the use of the asset (usufruct). Final redemption can be mad from the sale of the asset to the *mudharib.*

In Figure 2, As SPV generate funds from investors (point 2), then SPV can buy an asset from vendors/manufacturers (point 3). As SPV now the owner of an asset, then it can lease the asset for productive purposes to a company. Because the basis of this transaction is *ijarah* (leasing), company must pay the periodic lease payment to SVP (point 5). This payment then passed through to investors as their returns of sukuk (Bacha and Mirakhor, 2013).

D. Some Issues

In Islamic equities market, especially in stock market after the emergence of behavioral finance theory, Kazak, *et al.* (2024) explained the focus of research about the effect of global risk factors on stock returns and stock market volatility. Volatility of stock market is very crucial and valuable to be predicted for individual investors, investment institutions, and financial regulatory authorities in many fields such as portfolio selection, asset pricing, and risk management (He, *et al.* 2024). As in the current situation capital market is more liberalized, the global risk factors become the main focuss of the research related to Islamic capital market.

In Kazak, *et al* (2024)'s study, economic instability indicators such as economic policy uncertainty (EPU), Geopolitical risk, VIX, and others have an impact on Islamic equity market indices both in world and Turkey. They also found that VIX fear index become most important uncertainty variable to effect the Dow Jones Islamic Market World, and also in Turkish equity market. Therefore, it is crucial for policymakers to carefully track these indicators of instability and take appropriate actions. Investors should also take financial uncertainty indicators into account when shaping their investment strategies. For further research, Kazak, *et al.* (2024) suggested to include others countries with updated literature and with new econometric method.

In *sukuk,* one important issue now emerge is *cash-waqf linked sukuk* or CWLS. Official website of BWI (*Badan Waqf Indonesia*) explained that Cash Waqf Linked Sukuk is a form of social investment in Indonesia, where the cash waqf collected by the Indonesian Waqf Board (Badan Wakaf Indonesia) as the Nazhir, through BNI Syariah and Bank Muamalat Indonesia as Islamic Financial Institutions for Receiving Cash Waqf (LKSPWU), will be managed and placed in State Sukuk or State Sharia Securities (SBSN) issued by the Ministry of Finance.

Because this instrument is relatively new, the factors that determine potential investors to invest in this instrument is very essential to be studied. If the study is directed to study intention, then *Theory of planned behavior* could be best to explain the intention. To determine probability of independent variable to affect the emerge of intention to invest CWLS, then probit-logit model with dependent variable 1 or 0 might be important to be considered. If the research is directed to design the concept of cash waqf, ones can refer study conducted by Hasibuan and Lubis (2024) that aim to develop the halal food sector and the Islamic financial sector by integrating the halal value chain into the establishment of a food court financed through the cash Waqf linked sukuk (CWLS) Islamic financial instrument

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ISLAMIC MICRO FINANCE

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A. Introduction

In general, microfinance institutions (MFIs) are institutions that serve microfinance. Sharia microfinance institutions are financial institutions whose main business is to provide credit and other services in payment traffic and money circulation that operate in accordance with sharia principles. In a more in-depth discussion, understanding the meaning of financial institutions can at least be understood from what is stated in the Big Indonesian Dictionary, which gives the understanding that a Financial Institution is ‘a body in the financial sector whose job is to attract money and channel it to the public’.

The same thing is also contained in Law Number 14 of 1967 concerning Banking Principles, both conventional and sharia, which explains Financial Institutions are ‘all bodies that carry out activities in the financial sector by withdrawing money from the public and channeling the money back to the public’.

From the above definition, when associated with the word ‘sharia’ it can be understood that Sharia Financial Institutions are bodies that carry out activities in the financial sector by withdrawing money from the public and channeling the money back to the public using sharia principles. The word ‘micro’ in the mention of Sharia Microfinance Institutions, gives more meaning to the level of scope or smaller scope. With the comparative assumption that one of the large financial institutions is in the form of a bank with large-scale capital, microfinance institutions are other formations of banks or the like that have small capital and are intended for the small micro business sector. In this sense, Baitul Mal Wattamwil (BMT), Sharia Cooperatives and Sharia People's Credit Banks (BPRS) are categorised.

Microfinance is the provision of various forms of financial services including credit, savings, insurance and money transfers to poor, low-income individuals or families, and their micro-enterprises. This definition emphasises the broadening of the range of financial services previously associated with microcredit alone, and the targeting of poor or low-income people. Two key features of microfinance that distinguish it from formal financial services products are the small size of loans or deposits, and the absence of collateral in the form of assets.

Microfinance services can be provided by microfinance institutions, which are institutions whose main activity is to provide microfinance services, formal financial institutions that have microfinance service units, development programmes or poverty reduction programmes that have a microfinance component, and informal organisations formed by the community itself. Sharia microfinance is a terminology used in general terms, but sharia microfinance is better known as BMT.

The position of LKMS, better known as BMT, is very important because its existence is able to reach all sectors, including the middle and lower economic sectors, which in fact have many problems. According to Jenita: 2010 that however, the target or segment of Microfinance Institutions is always in contact with relatively poor or low-income people. In the midst of the development of financial institutions labelled as sharia banks in recent years, it has become one of the good signals of the continued rapid development of financial institutions that use sharia principles. Empirically, as an initial illustration, what is very interesting about the growing number of Islamic microfinance institutions is that the problem of financial support faced by the majority of this nation (especially farmers) will be resolved if the role of Islamic MFIs can be optimised.

In an empirical study conducted in Gunung Kidul-Jogjakarta by the InterCafe research institute of IPB in collaboration with CIFOR, it was found that the majority of farming communities living in rural areas, prefer arisan groups or cooperatives (45.5 per cent), whose practices are based on profit sharing and in accordance with local culture, when asked the preference of institutions to be approached as a solution to the financial problems faced.

From the above, it can be understood that the position of Islamic microfinance institutions in the economy is quite important and has the potential to be developed in all sectors. With the support of a large Muslim population, this will certainly not be impossible to do.

B. Overview of Islamic Microfinance Institutions in Indonesia

The development of Islamic microfinance institutions, especially in the last decade, both in terms of the number of institutions and the number of customers, has been remarkable. This is inseparable from the growing public awareness of the benefits and importance of carrying out economic activities through these financial institutions to achieve better conditions. It is even predicted that MFIs will have a strategic role in accelerating the process of Indonesia becoming a developed country by 2030. As stated by Chairul Tanjung, a businessman who is also the Chairman of the National Economic Committee (KEN), in his lecture at the 47th Anniversary of Bogor Agricultural University (IPB). He believes that Indonesia will be among the five largest developed countries by 2030 with MFIs being one of the main pillars.

Poverty alleviation programmes through Microfinance Institutions (MFIs) have actually been implemented in many developing countries. This programme is a means to assist small and medium entrepreneurs in financing investment for economic activities, reducing vulnerability to external shocks, consumption expenditure, and enabling the arbeitlose (unemployed) to become entrepreneurs when wage opportunities in the formal sector of the economy are limited. Even the United Nations explicitly declared 2005 as the beginning of the International Year of Microfinance, recognising that it is an important means of reducing world poverty.

In the Islamic concept, any country that has a clear goal, namely the formation of a prosperous society as stated by Imam al Syatibi in his work al muwafaqat fii alushul, will try to consistently seek and carry out various economic activities that are profitable and in accordance with the charar of the nation. Islamic Microfinance, which includes BMT, Sharia Cooperatives, BPRS and Islamic banks with their micro business units, is expected to help realise this goal. PINBUK itself, as an institution that accommodates BMT institutions in Indonesia.

C. Islamic Microfinance Institutions Theoretically (Theory and Role)

SMFI is a profit motive institution that is also social motive, whose activities are more community development in nature without ignoring its role as a financial intermediary institution that certainly uses Islamic values in its business activities. As a financial institution that functions as an intermediary institution, MFIs also carry out savings and loan activities, whose activities in addition to providing loans are also required to provide awareness of saving and caring for others through Islamic philanthropy to the community, especially low-income people. Theoretically, these parts will be explained as follows:

1. BPRS (Syariah Rural Bank)

According to Banking Law No. 7 of 1992, BPR is a financial institution that accepts money deposits only in the form of time deposits savings, and or other forms that are equated in that form and distributes funds as a BPR business. In Banking Law No. 10 of 1998, it is stated that BPR is a bank financial institution that carries out its business activities conventionally or based on sharia principles. The regulation of the implementation of BPRs that use sharia principles is contained in the letter of the Board of Directors of Bank Indonesia No. 32/36/KEP/DIR / concerning Rural Banks Based on Sharia Principles dated

12 May 1999. In this case, Islamic BPR technically operates like conventional BPR but uses sharia principles.

The objectives of establishing BPR Syariah are:

a. Improving the economic welfare of the Muslim community, especially the economically weak people who are generally in rural areas.
b. Increase employment opportunities, especially at the sub-district level so as to reduce the flow of urbanisation.
c. Fostering the spirit of ukhuwah islamiyyah through economic activities in order to increase per capita income towards an adequate quality of life.

To achieve the operational objectives of BPR Syariah, an operational strategy is needed, namely:

a. BPR Syariah is not waiting for requests for facilities but is active by conducting socialisation/research to small-scale businesses that need additional capital assistance, so that they have good business prospects,
b. BPR Syariah has a type of business that has a short-term turnover time by prioritising medium and small-scale businesses.
c. BPR Syariah examines the market share, the level of saturation and the competitive level of the product to be given financing.

2. Baitul Maal Wattamwil (BMT)

BMT is a concise designation of the Sharia Microfinance Institution Baitul Maal wat Tamwil or Balai-usaha Mandiri Terpadu, a Sharia Microfinance Institution (LKMS) that combines economic and social activities of the local community. Baitul Maal Wattamwil (BMT) is a self-help group as a people's economic institution that seeks to develop productive and investment businesses with a profit-sharing system to improve the economic quality of small and small entrepreneurs in poverty alleviation efforts. LKMS BMT activities are to develop productive economic enterprises by encouraging saving activities and assisting the financing of economic business activities of members and their neighbourhood communities. LKMS BMT can also function socially by raising deposits of social funds for the benefit of the community, such as zakat, infaq and sodaqoh funds and distribute them with the principle of community empowerment in accordance with the rules and mandates.

The purpose of BMT is to improve the quality of economic businesses for the welfare of members in particular and society in general. While the nature of BMT is to have a business venture that is independent, grown with self-help and managed professionally and orientated to the welfare of members and the community environment. BMT can be established and developed with a gradual process of legal legality. Initially it can be started as a self-help group by obtaining a certificate of operation / partnership from PINBUK (business incubation centre for small and medium enterprises) and if it has reached a certain asset value immediately prepare themselves into a cooperative legal entity.

BMT has the following characteristics:

a. Business-oriented, seeking mutual profit, increasing the utilisation of the lowest economy for members and the environment.
b. Not a social institution but used to activate the use of social donation funds, zakat, infaq and sadaqah for the welfare of many people in a sustainable manner.
c. Grown from below based on the role of participation from the surrounding community, owned by the local

community from the BMT NGO environment itself, not owned by others from outside the community.

The role of BMT in the community includes:

a. Economic and social motor of many communities.
b. The spearhead of the implementation of the sharia economic system.
c. Liaison between the *aghnia* (rich) and the *dhu'afa* (poor).
d. Means of informal education to realise the principle of a barakah life.

When viewed within the framework of the Islamic economic system, the purpose of BMT can play a role in doing the following:

1. Help improve and develop the potential of the people in poverty alleviation.
2. Make an active contribution to efforts to empower and improve the welfare of the people.
3. Creating a source of financing and providing capital for members with sharia principles.
4. Developing a frugal attitude and encouraging savings.
5. Developing productive businesses and at the same time providing guidance and consultation for members in their business fields.
6. Increase the insight and awareness of the ummah about Islamic economic systems and patterns.
7. Helping weak entrepreneurs to get capital and loans.
8. To become an alternative financial institution that can support the acceleration of national economic growth.

The functions of BMT in the community include:

1. Improve the quality of human resources of members, administrators, and managers to be more professional,

greetings, and trustworthy so that they are more intact and resilient in struggling and trying to face global challenges.

2. Organising and mobilising funds so that funds owned by the community can be optimally utilised within and outside the organisation for the benefit of the people.
3. Developing employment opportunities.
4. Strengthen and improve the quality of business and market products of members, strengthen and improve the quality of economic and social institutions of the people.

Conceptually BMT has two functions, namely:

1. *Bait at-tamwil* (bait means house, *attamwil* means property development) conducts productive business development activities and investment in activities to improve the economic quality of micro and small entrepreneurs, especially by encouraging saving activities and supporting the financing of economic activities.
2. *Bait al-mal* (bait means house, *al-mal* means treasure) receives deposits of zakat, *infaq* and *sadaqah* funds and optimises distribution in accordance with its mandate.

D. Conclusion and Recommendation

Theoretically the role of MFIs acts as a financial and social institution that is able to empower small communities and overcome socio-economic problems such as poverty etc. In empirical practice, the role of SMFIs has maximally positioned itself as a financial and social institution. But there are still many obstacles that surround it such as lack of human resources, information, and public trust, as well as the development of other financial institutions that are increasingly modern.

Some recommendations that can be a contribution to the development of sharia microfinance institutions are as follows:

1. **Paradigm Transformation about Sharia Microfinance Institutions.**

   There are some people who still do not trust and do not understand the mechanism of SMFI. Knowledge of Islamic insurance must be socialised to the community, both the general public and small communities. The benefit is that the general public will better understand and believe in SMFIs and it is possible to use SMFI products.

   This has implications for the increase in tabarru' funds collected for benevolence that will help and empower the poor. In addition, small communities who initially did not know became aware of the advantages and benefits of MFIs. It also encourages small communities to do business and become objects of empowerment. Overall, the benefit of this paradigm shift is to help the community how important it is to live productively in the context of mutual help in accordance with sharia principles.

2. **Improving SMFI Cooperation with Various Parties**

   In facing the constraints of limited access of small communities to capital, SMFIs should increase more intensive cooperation with BUMDES in order to optimise the program and achieve product targets. BUMDES is the agent or distributor of SMFI for small communities. The more SMFIs cooperate with BUMDES, the more poor people can be assisted and empowered. In addition, cooperation between SMFIs, and LAZ or BAZNAS needs to be improved and promoted. Good cooperation between SMFIs that specifically serve the poor, and LAZ (Lembaga Amil Zakat) or BAZNAS will make it easier for the poor to get access to productive assistance or capital, for example the poor can participate as mustahik participants managed by LAZ from zakat and infaq and sodaqoh sources.

3. Product Development of SMFIs

SMFIs should have more diverse products that can attract people to use the services of this institution or invest. In addition, SMFIs should also increase the number of micro sharia products that can be accessed by small communities. The diversity of these products, especially products for small communities, will greatly help small communities. In addition, SMFIs must innovate in technology in the management of their institutions so that they do not lose out on competing with financial institutions that have developed in accordance with technological developments.

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OPPORTUNITIES AND CHALLENGES IN ISLAMIC ECONOMICS

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A. Introduction

Islamic economics is a comprehensive system of thought that offers an alternative to the secular, capitalist economic frameworks that dominate the global economy today. Rooted in Sharia law, Islamic economics emphasizes principles such as social justice, ethical investment, and the equitable distribution of wealth. In contrast to the profit-maximizing motives inherent in capitalism, Islamic economics seeks to align economic activities with moral and ethical values prescribed by Islam, aiming to create a balanced and just society. However, in a world largely governed by secular liberal capitalism, the application of Islamic economics presents both challenges and opportunities. The current economic landscape, characterized by market-driven policies, income inequality, and environmental degradation, highlights the need for alternative economic models that prioritize social welfare and sustainability—principles that are central to Islamic economics (Haneef & Mirakhor, 2021).

Recent years have witnessed significant advancements in the field of Islamic finance, which forms a critical component of Islamic economics. Islamic finance has grown rapidly, offering a range of financial products that adhere to Sharia principles, such as sukuk (Islamic bonds), takaful (Islamic insurance), and Sharia-compliant investment funds. These products have gained traction not only in Muslim-majority countries but also in global financial markets, reflecting a growing demand for ethical and socially responsible investment options. Moreover, the integration of Islamic finance with global sustainable development goals (SDGs) and Environmental, Social, and Governance (ESG) criteria represents a cutting-edge development that bridges the gap between Islamic ethical values and contemporary global concerns (Abdullah & Ismail, 2020). The rise of Islamic fintech, offering innovative financial solutions that align with both Islamic law and modern technology, further illustrates the dynamic evolution of this field (Ahmed, 2021).

Despite these advancements, there remains a significant challenge in understanding how Islamic economics can be effectively implemented within the existing secular, capitalist economic framework. The majority of studies have focused on the growth and performance of Islamic financial products in isolation, without adequately addressing the broader challenges of integrating Islamic economic principles into a global system dominated by liberal capitalism.

Moreover, there is limited research on the long-term sustainability of Islamic finance when it operates within a secular framework that often conflicts with its ethical and moral foundations. This gap is particularly pronounced in the areas of policy formulation, regulatory frameworks, and the practical implications of adopting Islamic economic principles on a global scale (Rahman & Shahin, 2020).

This chapter seeks to bridge the gap by exploring the potential of Islamic economics to offer a viable alternative to the secular, capitalist system that currently prevails. By examining the application of Islamic financial products in the context of global capitalism, this study will provide insights into the opportunities and challenges of integrating Islamic economic principles into a predominantly secular economic framework. Additionally, this research will contribute to the ongoing discourse on ethical and sustainable finance by highlighting how Islamic finance can complement and enhance global efforts to achieve economic justice and environmental sustainability. Ultimately, this study aims to advance the understanding of how Islamic economics can be both a practical and ethical alternative to the current global economic system, offering solutions that address the limitations and inequalities inherent in liberal capitalism (Haneef & Mirakhor, 2021; Abdullah & Ismail, 2020).

B. Opportunities for Islamic Economics

1. Leveraging Ethical Finance for Broader Appeal

Islamic finance, with its ethical foundation, presents a unique opportunity to appeal to a broader audience in the secular liberal capitalist system. The growing global interest in ethical and socially responsible investing aligns well with Islamic principles that prohibit riba (interest) and emphasize risk-sharing and social justice. This convergence offers Islamic finance a platform to expand beyond its traditional markets, attracting non-Muslim investors who are increasingly concerned with the social and environmental impacts of their investments. The ethical framework of Islamic finance could thus serve as a bridge between Islamic economics and global financial markets, fostering greater acceptance and integration within the secular system (Abdullah & Ismail, 2020). In a future Islamic system, this foundation could evolve from a niche appeal to a comprehensive economic model that governs all financial activities, ensuring that the principles of justice and equity are deeply embedded in every transaction.

2. **Promoting Social Welfare through Islamic Social Finance**

   The integration of Islamic social finance instruments like zakat, waqf, and sadaqah within a secular capitalist system offers a novel approach to addressing poverty and inequality. These instruments can be institutionalized within existing welfare systems to enhance social safety nets and provide more targeted support to the most vulnerable populations. By positioning Islamic social finance as a complement to state welfare programs, Islamic economics can demonstrate its relevance and adaptability in addressing modern social challenges (Ahmed, 2021). In a future Islamic system, these instruments would not merely supplement welfare programs but would be central to the economic structure, ensuring a systematic approach to wealth redistribution that upholds the principles of social justice and community welfare.

3. **Utilizing Islamic Fintech for Financial Inclusion**
   The rise of financial technology (fintech) presents an opportunity for Islamic economics to advance financial inclusion, particularly in regions underserved by traditional banking systems. Islamic fintech platforms, which offer Sharia-compliant financial services, can leverage technology to reach wider populations, including those in remote or marginalized communities. This approach aligns with the ethical and inclusive nature of Islamic finance, providing a practical solution to the challenges of financial exclusion within a secular capitalist system (Haneef & Mirakhor, 2021). In a future Islamic system, Islamic fintech could play a pivotal role in ensuring that all members of society have access to financial services that are aligned with Islamic values, thereby supporting broader economic participation and social equity.

4. **Aligning Islamic Finance with Sustainable Development Goals (SDGs)**
   Islamic finance's emphasis on ethical investment and social responsibility aligns closely with the United Nations' Sustainable Development Goals (SDGs). This alignment offers an opportunity for Islamic finance to contribute meaningfully to global sustainability efforts within the secular capitalist framework. By focusing on green sukuk (Islamic bonds) and other Sharia-compliant financial instruments that fund sustainable projects, Islamic economics can position itself as a leader in the global push for sustainable development (Rahman & Shahin, 2020). In a future Islamic system, the principles of sustainability would be fully integrated into the economic model, ensuring that development is pursued in a way that preserves

environmental integrity, promotes social justice, and fulfills the maqasid al-shariah (objectives of Islamic law).

5. **Developing Alternative Economic Models through Hybrid Systems**
   One out-of-the-box opportunity for Islamic economics within a secular capitalist system is the development of hybrid economic models that blend Islamic principles with elements of capitalism. These models could serve as transitional frameworks, gradually introducing Islamic economic principles into mainstream economic practices. For example, profit-sharing models in corporate governance could be introduced alongside conventional capitalist structures, providing a pathway towards a more ethical and socially responsible business environment (Dusuki, 2019). In a future Islamic system, these hybrid models could be further refined and expanded, eventually leading to a comprehensive economic system that fully embodies Islamic values while remaining competitive in a globalized world.

6. **Innovating Islamic Microfinance as a Global Tool for Poverty Alleviation**
   Islamic microfinance presents a unique opportunity to address global poverty by offering interest-free loans and profit-sharing arrangements to low-income individuals and entrepreneurs. This approach not only aligns with Islamic principles but also offers a viable alternative to the often exploitative practices of conventional microfinance in a secular capitalist system. By scaling Islamic microfinance initiatives globally, Islamic economics can demonstrate its potential to offer ethical, effective solutions to poverty that resonate across different cultural and religious contexts

(Ahmed, 2021). In a future Islamic system, Islamic microfinance would be a cornerstone of economic development, promoting entrepreneurship and financial independence while adhering to the principles of justice and fairness.

C. Challenges in Islamic Economics

1. Cultural Resistance to Change

Implementing Islamic economics within a secular capitalist system faces significant cultural resistance, even within Muslim-majority countries that have adopted capitalist values. The secular capitalist ethos, which emphasizes individualism, consumerism, and profit maximization, contrasts sharply with the communal welfare, ethical constraints, and social justice that are central to Islamic economics. This resistance is compounded by the global dominance of Western cultural norms that prioritize personal freedom and material success. Recent studies have highlighted the difficulties in shifting societal values towards a more collective and ethically grounded economic model, particularly when these values are deeply entrenched in capitalist societies (Abdullah & Ismail, 2020; Rahman & Shahin, 2020). In a future Islamic economic system, the challenge would be to cultivate a cultural environment where Islamic economic values are naturally integrated into daily life, rather than perceived as an imposed shift.

2. Technological Disruption and Ethical Dilemmas

The rapid advancement of technology in the secular capitalist system introduces new financial instruments and practices—such as cryptocurrencies, blockchain, and AI-driven finance—that pose significant ethical dilemmas for

Islamic economics. These technologies often operate in ways that challenge traditional Islamic legal frameworks, creating difficulties in ensuring they comply with Sharia principles. Scholars have noted the complexity of adapting Islamic jurisprudence to these emerging technologies, particularly in a system where profit and innovation are prioritized over ethical considerations (Ahmed, 2021; Haneef & Mirakhor, 2021). In a secular capitalist environment, Islamic finance must navigate these disruptions without compromising its core values. Conversely, in a future Islamic economic system, the task would be to proactively guide technological innovation to align with Islamic ethics, ensuring that new technologies support the principles of fairness, justice, and equity.

3. **Global Geopolitical Dynamics**

The implementation of Islamic economics within the secular capitalist global system is complicated by geopolitical challenges. The current global financial architecture, dominated by secular states and international organizations, may resist the rise of Islamic finance, viewing it as a challenge to the established order. This resistance could manifest through policies that undermine the growth of Islamic financial institutions or through strategic moves to limit their influence (Dusuki, 2019; Haneef & Mirakhor, 2021). In a future Islamic economic system, the challenge would shift to establishing a new global order where Islamic economics is not merely a regional phenomenon but a central pillar of the global economy, requiring diplomatic and strategic efforts to gain international acceptance and cooperation.

4. **Environmental Crises and Resource Scarcity**
   Environmental challenges, such as climate change and resource scarcity, present significant obstacles to implementing Islamic economics in a secular capitalist system. While Islamic economics emphasizes sustainability, the practical application of these principles is often at odds with the profit-driven motives of capitalism. Recent research highlights the difficulty of integrating Islamic principles of environmental stewardship into a system that prioritizes short-term gains over long-term sustainability (Rahman & Shahin, 2020; Abdullah & Ismail, 2020). In the secular capitalist context, the challenge is ensuring that Islamic economic practices can influence broader environmental policies and market behaviors. In a future Islamic economic system, the focus would need to be on creating an economic framework where sustainability is not just a policy goal but an integral part of every economic activity, ensuring that economic growth does not compromise social justice or environmental sustainability.

5. **Hybrid Economic Models and Identity Crisis**
   As Islamic economics seeks to integrate with the secular capitalist system, there is a risk of creating hybrid models that dilute its core principles. These hybrids may blend Islamic finance with conventional capitalist practices, leading to a potential identity crisis where the unique ethical foundations of Islamic economics are compromised. Scholars have expressed concerns that these hybrid models could result in a superficial adherence to Sharia principles, while fundamentally operating within the capitalist ethos (Ahmed, 2021; Abdullah & Ismail, 2020). In a secular capitalist system, the challenge is to maintain the

integrity of Islamic economics while making it compatible with global markets. In contrast, in a future Islamic economic system, the challenge would be to resist external pressures to conform to global capitalist norms and instead develop a distinct and robust economic identity that remains true to Islamic values.

6. **Ethical Fatigue in a Hyper-Commercialized World**
   The secular capitalist system's relentless focus on commercial success can lead to "ethical fatigue," where the continuous emphasis on ethical considerations in finance becomes burdensome. This fatigue can result in a gradual erosion of commitment to ethical principles, as individuals and institutions prioritize short-term financial performance over long-term ethical integrity. Recent studies suggest that in a hyper-commercialized environment, maintaining a commitment to ethics in finance becomes increasingly challenging, as market pressures often lead to compromises (Rahman & Shahin, 2020; Dusuki, 2019). In a secular capitalist context, this presents a challenge for Islamic finance to maintain its ethical rigor. In a future Islamic economic system, the challenge would be to embed ethical practices so deeply within the economic framework that they are seen not as optional or burdensome, but as integral to economic success and societal well-being.

These challenges illustrate the complexities of implementing Islamic economics within a secular capitalist framework and the distinct obstacles that would be encountered in establishing a future Islamic economic system. Addressing these issues will require not only economic and legal innovation but also a cultural shift and strategic geopolitical positioning to ensure that Islamic economics can thrive both within and beyond the constraints of the current global system.

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CONTEMPORARY ISSUES & DEVELOPMENTS IN

ISLAMIC ECONOMICS

Contemporary Issues & Developments in Islamic Economics is an insightful exploration into the foundational principles and progressive applications of Islamic economic thought. The book covers a wide spectrum, from fundamental Islamic finance concepts to specialized areas such as Islamic banking, capital markets, and microfinance. Each chapter offers an in-depth analysis of how Islamic economics distinguishes itself with principles of justice, transparency, and shared prosperity. The discussions are accessible yet thorough, making the book an excellent resource for students, academics, and professionals interested in the evolving landscape of Islamic economics.

The final sections of the book address modern challenges and opportunities in Islamic economics, considering global shifts like digitalization and financial technology. This reflection on current trends makes the book particularly valuable for understanding how Islamic economic principles can adapt to contemporary needs. By bridging historical foundations with modern applications, Contemporary Issues & Developments in Islamic Economics provides readers with a comprehensive understanding of the field's unique potential to contribute to equitable and sustainable economic solutions on a global scale.

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